



December 1995
RG-80 (formerly LP 92-21)

Water District Accounting Manual 1995 Edition

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1995 Edition

Prepared by

Water Utilities Division
Texas Natural Resource Conservation Commission

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December 1995

INTRODUCTION

A. PURPOSE OF THE *MANUAL*

The Water District Accounting Manual (Manual) is primarily designed to accomplish the following objectives:

1. To provide minimum standards for maintaining fiscal records in compliance with Texas Water Code §49.196.
2. To guide districts in establishing an accounting system which meets the management needs of the district.
3. To provide a reference source for evaluating the adequacy of the district's accounting system for use by the members of the board of directors and district personnel who supervise accounting functions.
4. To provide a reference source for independent auditors who must evaluate and report on the internal control system.

B. LEGAL STATUS OF *THE WATER DISTRICT ACCOUNTING MANUAL*

Texas Water Code §49.192 authorizes the executive director of the Texas Natural Resource Conservation Commission to adopt accounting and auditing manuals. The manuals referred to in §49.192 include two separate publications:

1. *The Water District Accounting Manual (Manual)* is this publication which primarily addresses the accounting function of the district, including unaudited reports to the board of directors.
2. *The Annual Audit Reports Requirements (AARR)* is considered to be a part of the *Manual* and is to be used in conjunction with the *Manual*. It specifies the financial reporting requirements of districts as addressed in the annual audit process. The *AARR* applies to all districts, although the levels of reporting may vary according to the type and function of the district. The *AARR* will be updated as audit report requirements change.

Texas Water Code §49.196 requires that all fiscal records of the district be prepared on a timely basis and maintained in accordance with generally accepted accounting principles (GAAP). The *Manual* intends to describe the minimum attributes of an accounting system which would comply with that statute.

Texas Water Code §49.195 provides that the Commission may review the audit report of each district. If violations of generally accepted auditing standards (GAAS), accounting principles, statutes or Board rules are noted, or if the executive director (ED) has any recommendations, the ED is required to notify the board and the district's auditor. The ED may also inspect the records of the district. The *Manual* is

intended to be an aid to the board of directors and its consultants. It is the responsibility of the district's board, contractors, consultants and independent auditor to be aware of and to implement any changes in applicable statutes, rules, GAAP and GAAS.

Texas Water Code §49.199 requires that each district adopt certain administrative policies and a code of ethics. An example of such policies are included in **Appendix O**. We recommend that each district also consider the adoption of an administrative manual to address procedural and accounting issues which are specific to the district. This *Manual* is not intended to supplant any manual adopted by the board to direct the administrative processes of the district.

C. LEGAL ENVIRONMENT OF DISTRICTS

Districts authorized by the Texas Constitution derive specific powers and duties from special laws enacted by the legislature or from general laws as set forth in the Texas Water Code. Special law districts must refer to their enabling legislation, and any amendments thereto, to determine which provisions prevail over the Water Code statutes. Most legislation for special law districts also refers to the applicable general law by which those districts are governed.

Districts must refer to the Tax Code, Election Code, Local Government Code, bond resolutions and other legal restrictions in addition to the Water Code in determining their legal environment. **The *Manual* will not provide guidance for legal compliance.** That guidance should be provided by the district's attorney who can interpret the law according to the specific situation of the district.

D. DISTRICTS SUBJECT TO THE *MANUAL*

The *Manual* applies to all districts and authorities created under either Article III, Section 52, {Subsection (b), Subdivisions (1) and (2)}, or Article XVI, Section 59, of the Texas Constitution.

There are no exceptions to the applicability of the *Manual*. In the past, river authorities were granted exemption by an order of the Texas Water Rights Commission dated April 8, 1975. This exemption was granted to river authorities because they had the option to be audited by the State Auditor to satisfy the requirement for an annual audit. However, this option was removed in 1989 by the 71st Legislature. Therefore, the exemption from the *Manual* formerly granted to river authorities is no longer extended.



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I. OVERVIEW OF THE ADMINISTRATIVE SYSTEM

A. OBJECTIVES

The administrative system of a district includes its accounting system, the maintenance of non-accounting records, employee and consultant relations, and other management concerns. The purposes of an effective administrative and management system for districts include four important functions:

- > safeguarding of assets
- > planning and control
- > demonstrating legal compliance
- > timely reporting

1. Safeguarding of Assets

The board of directors is responsible for the stewardship and protection of the district's assets. The assets may include all cash, accounts receivable, investments, inventories, supplies, equipment, buildings, and infrastructure. The administrative system must identify and quantify those assets to ensure accountability. The board must also ensure that the assets are not used unnecessarily or for non-district purposes.

2. Planning and Control

An efficient administrative system facilitates the district's ability to manage its resources and plan for future events. The accounting system should provide meaningful and accurate reports for use in controlling operations. Records should be available to inform the board of past operations, contract provisions and historical trends. The guidelines for employees and by-laws of the district should provide for the accountability of employees while on official duty. The duties of consultants should be specified by contract and monitored on a periodic basis.

Proper planning and control is greatly facilitated by the budgetary process. Texas Water Code §49.199 (a)(6)(A) requires the adoption of a formal budget by the board. The formal budget should be used to help control expenditures and as a reference for decision making. It may also be used as a spending limitation for management should it be determined that it is in the best interest of the district.

3. Demonstrating Legal Compliance

Another primary concern of the district is compliance with Texas statutes, federal laws and mandates, contractual provisions (including bond orders), and with the by-laws and board resolutions of the district. The record keeping system must retain the key records of the district and ensure that they are accessible to management and the board. The accounting system must ensure that funds are separated as appropriate and used in accordance with authorizations. The personnel and consultant management system must be able to document compliance with federal mandates and contractual agreements.

4. Timely Reporting

Each district is accountable to the public, supervising state agencies, bondholders, and other interested parties. The ability to provide timely reports to these parties is a crucial element in managing a district.

The administrative system must ensure that the data required for the annual audit and other reports is captured by the accounting system and that procedures are in place to submit the reports on a timely basis.

B. OVERVIEW OF THE ACCOUNTING PROCESS

1. Checks And Balances

The accounting system must capture and quantify each change in assets, liabilities and fund balance. This is done by a double-entry system of bookkeeping which ensures that for each transaction, the effect on assets is balanced by a corresponding effect on liabilities or fund balance. (The fund balance is the net cumulative effect of operating results - similar to “retained earnings” in private-industry accounting.) Simply stated, for every debit or credit entry there must be a corresponding credit or debit entry to an appropriate account.

At the end of an accounting cycle, the debits and credits are balanced to ensure that the double-sided effect of each transaction has been recorded. For example, any change in cash must have a corresponding entry for the source or use of that cash. A change in cash without a corresponding entry would be a cause for further investigation.

There are a variety of accounting systems and methods, both in manual and automated formats. However styled, an accounting system typically has the following basic books:

- > a general ledger,
- > general and/or specialized journals (or transaction register), and
- > a chart of accounts.

The use of these books provides the foundation for the system of recording, classifying and reporting accounting information.

2. The Accounting Cycle

The accounting process gathers and summarizes comprehensive financial data in a clear and concise manner with the intention of organizing the resulting information in a way that enables responsible personnel to better perform their assigned duties.

The primary foundation of an accounting system is the **Chart of Accounts**. This document determines how data is classified and summarized for future reporting. For instance, if the expenditure accounts are defined only as “other” and “miscellaneous,” much significant detail would be lost as many different types of transactions will be merged together in the summaries.

The Chart of Accounts should provide a balance in the level of detail. A very detailed system of accounts will provide more information on specific transactions. However, working with a large number of accounts may be too unwieldy for the benefits gained. Most systems provide for summary accounts which consolidate a number of more finely defined accounts. In this way, the details are not lost and the summaries can be used for reporting purposes. An example Chart of Accounts is included in **Appendix G**.

The Chart of Accounts should be accessible to all employees involved in authorizing, classifying, and recording financial data. Since the Chart of Accounts provides the guidance for how data will be classified, it is only valid if the use of each account is consistent throughout the organization.

The financial data to be organized originates from **source documents**. These documents provide supporting or underlying evidence for all financial transactions. Examples of source documents include purchase invoices, billing stubs, and cash receipt slips. Since source documents are often the only tangible evidence of a financial transaction, they should be filed in a consistent and logical manner for future reference.

Source documents received from or verified by external parties provide more reliable evidence of accounting transactions than internally-generated documents. For example, a cash receipt slip signed by the recipient is preferable to a cash receipt slip signed only by district personnel. When it is not possible to obtain external evidence of a transaction, a statement as to the nature of the transaction, the authorization and any contact persons should be included in the records and cross-referenced in the journals.

The original book of entry of a transaction into the accounting system is usually in a journal (or a **transaction register** for computerized systems). The journals may be highly specialized for the specific type of transaction, or they may be more generic to capture a variety of transactions. The purpose of the journals is to provide a chronological listing of all transactions and how the transactions are classified into accounts, with sufficient references to the source documents to allow for ready retrieval. The journals allow for common transactions to be summarized on a periodic basis before posting to the general ledger.

For instance, service receipts from customers would be journalized in such a way that each service account affected is listed, with a summary total of cash received (a debit) and summary total of credits to the customer accounts. The total cash received should correspond with the total on the deposit slip recorded by the bank. The increase in cash (a debit) is posted to the **General Ledger** to the appropriate cash account, and the decrease in accounts receivable from customers (a credit) is posted to the **General Ledger** account which summarizes the individual account balances.

A check register can act as a **Cash Disbursements Journal** if it is sufficiently detailed to provide a cross-reference to the supporting documentation and to the accounts affected by the transaction. The account totals are periodically summarized and posted to the general ledger.

The purpose of the **General Ledger** is to organize and summarize the individual transactions listed in the journals. The General Ledger is broken down into the account categories which are listed in the Chart of Accounts. The summary totals from the journals are posted to the general ledger so that the effect of transactions on each account category can be readily determined. The General Ledger should cross-reference to the journals so that the transactions can be traced back to the source if necessary.

The General Ledger provides the basis for reporting financial information. All transactions recorded in the journals or by other means should be summarized in the General Ledger under the appropriate account category.

At the end of the accounting cycle, the General Ledger is balanced to ensure that the debits and credits are equal. This helps to determine errors in accounting, data entry, or of omission. However, a “balanced” set of books does not ensure that all transactions have been entered, that the transactions have been correctly classified, or that the transactions have been properly authorized.

3. **Authorization**

The most common transactions for water districts are simple receipts and disbursements of funds. Therefore, it is imperative that a formal authorization process be adopted to control the flow of funds into and out of the organization. Access to cash, both receipts and disbursements, should be limited to as few individuals as possible. In addition, the ability of any one individual to both initiate and complete any single transaction should be avoided.

The authority to disburse funds or to credit accounts should be traceable to the board of directors in some way. This could be in form of direct authorization of every expenditure by the board of directors or a resolution to authorize a certain party to disburse funds of up to a certain amount. In any case, all direct or indirect authorizations should be a result of board action at a public meeting and included in the board minutes.

Vouchers are often used to indicate the authorization and classification of a disbursement. **Vouchers** are a form attached to the source documents to capture key information necessary to process a disbursement, such as vendor name, vendor code (if any), authorizing initials or signatures, and classification of the transaction by account codes. This form may be used to indicate the date of the board meeting where the expenditure was approved, or other pertinent information associated with the transaction.

4. **Classification**

The function of classifying transactions is a key component in an accounting system. Transactions are usually classified according to the Chart of Accounts, typically in coded form for efficiency. The classification of transactions should be performed by the person(s) most familiar with the nature of the transaction when possible. All staff personnel who initiate or supervise disbursements should be familiar with the Chart of Accounts codes so that they can properly identify and classify the nature of the transaction.

5. **Segregation Of Duties**

An adequate accounting system will include a system of checks and balances. In addition to the precautions mentioned above concerning the receipt and disbursement of funds, procedures detailing a segregation of duties should be incorporated into any accounting system to the extent practicable.

A good example of segregation of duties is the separation of operational responsibility from recording responsibility. For example, a bookkeeper should not handle cash, nor should the cashier have access to ledger account records.

Segregation of duties and a formal authorization procedure are examples of elements of internal control. As the size and complexity of the accounting system increases so also should internal control procedures be enhanced to compensate.

6. **Internal Control**

The topics addressed above form a part of what is referred to as the **internal control** processes of an organization. The purpose of internal control procedures is to provide for the prevention and detection of errors and irregularities occurring in the normal course of business.

A checklist of internal control procedures applicable to small entities is in Section II-D. This is an example only and should be used for guidance only if applicable.

Your independent auditor can be a valuable source of information on the internal control system of the district. He should provide the governing board with an evaluation of the district's system of internal controls and recommendations for improvement. This is done by a **management letter** directed to the board of directors and submitted with the annual audit report. It is the responsibility of the governing board to consider the recommendations contained in the management letter and to direct changes in the current system if appropriate.

C. **MAINTENANCE OF ADMINISTRATIVE RECORDS**

Proper maintenance of administrative records has become increasingly important with the advent of legislation such as the Texas Open Records Act and the Texas Local Government Records Law. Water districts, as governmental bodies, are subject to the Texas Open Records Act which reads, in part, "all information collected, assembled, or maintained by governmental bodies pursuant to law or ordinance or in connection with the transaction of official business is public information and available to the public during normal business hours of any governmental body, with few exceptions."

Records that should be maintained by a water district include all accounting records; all engineering records; all records which involve bonds, taxes, contracts and insurance documents; inventory and cost records; legal records and documents; payroll and related personnel records; purchasing and receiving records; and so forth. A retention schedule should be maintained so that non-useful records may be destroyed on a systematic basis. The Texas Local Government Records Law defines this process. See **Appendix J** for a suggested records retention schedule.

The Texas Local Government Records Law

The Texas Local Government Records Law, enacted in 1989, requires that the district's board establish an active and continuing program for the creation, maintenance, and management of district records.

On or before January 2, 1995, the board should have designated a records management officer and established a records management program. Also, the records management officer should have prepared and filed with the Texas State Library, a records control schedule listing the retention period for each type of record.

D. BASICS OF FUND ACCOUNTING

1. Fund Concepts

Within the framework of accounting theory applicable to water districts there are two broad classifications of accounting entities:

- > the fund, and
- > a fund-like entity known as an account group.

A fund is defined as an independent accounting entity consisting of a self-balancing set of accounts containing only those asset, liability, fund balance, revenue and expenditure accounts necessary to reflect the financial results of some specific activity or the attainment of some objective. In other words, a fund has only those accounts necessary to reflect the specific operations for which the fund is established.

Account groups are defined as independent accounting entities consisting of self-balancing sets of accounts established to account for the fixed assets and/or the bonded debt of the water district. The emphasis of an account group is on accounting for either fixed assets or long-term liabilities and not on results of operations.

The distinction between a fund and an account group is merely one of definition, since the accounting treatment given to each type of entity is virtually the same. For purposes of the *Manual*, the term fund is used to refer to both funds and account groups.

2. Basis For Multi-Fund Accounting

Governmental entities in the State of Texas typically issue three types of bonds:

- > general obligation bonds,
- > revenue bonds, and
- > combination tax and revenue bonds.

General obligation bonds are secured by the taxing authority of the governmental entity. Revenue bonds are secured by a lien on revenues generated by providing services to users. Combination tax and revenue bonds are secured by both the general taxing authority of the governmental entity and are further secured by a lien on revenues generated by providing services to users.

Accounting for general obligation bonds requires that multiple funds be used. Separate funds must be established to account for bonded indebtedness, fixed assets, construction of fixed assets, debt service payments, operations of the governmental entity and any special revenues. These functions must be separately accounted for because each constitutes a separate function of the governmental entity as a whole.

Accounting for revenue bonds requires that a single fund be used. All activities accounted for in this single fund are directed toward the liquidation of the bonded debt for which the fund was established and for maintaining, thereafter, a nearly completely self-supporting enterprise type activity. Enterprise activities are usually sub-functions of a larger governmental entity. GASB Section 1300.104.b(1) states the appropriate circumstances for using such funds:

“b. Proprietary Funds

- (1) **Enterprise Funds** - to account for operations (a) that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expense incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.”

Although the decision of whether to use a proprietary or governmental fund type for district accounting is a governing board decision, the decision should be made in light of the full context of GASB Section 1300.104.b(1) and the related sources of generally accepted accounting principles. A district that finances all of its water and wastewater operations and discharges its liabilities through user charges could use a single enterprise fund in accordance with the previous quotation. A few districts utilize both proprietary funds and governmental funds.

Water districts are the primary issuers of combination tax and revenue bonds. These bonds are similar to general obligation bonds in that the primary security is the taxing authority of the water district. Repayment of the bonds and the interest expense is first attempted through service revenues. In the event that service revenues cannot meet the debt obligations of the district, tax revenues may be used to extinguish the debt.

Water districts are governmental entities. As such, they can perform several functions, not the least of which is providing water services. They are also authorized, in some cases, to provide:

- > sewage collection and treatment services,
- > fire protection,
- > construction and maintenance of recreational areas, and
- > other specific services as authorized by legislation.

In order to properly account for varied activities, water districts are compelled to use as many of the governmental funds and account groups as are necessary.

3. Governmental Funds and Account Groups

The following discussion briefly describes the purpose of each fund.

- a. **GENERAL FUND** - This fund is used to account for all transactions not included in any of the remaining funds. Normally, this fund includes accounts for most of the general revenues and expenses with supporting asset and liability accounts.
- b. **DEBT SERVICE FUND** - This fund serves to account for the receipt of revenues for and the payment of interest and principal on bonded debt. Other expenditures of this fund include the costs of:
 - > assessing property values,
 - > levying and collecting taxes, and
 - > fiscal agent fees.

Bond orders, an integral part of every bond issue, contain provisions and resolutions dictating how bond proceeds are to be used, and also, how revenues are to be generated. Therefore, it is important that the district's management seek professional advice and guidance from the district's attorney and certified public accountant on issues concerning bonds.

It is not unusual for the actual collection of taxes to be performed by a tax collector. In this event, the entries for the debt service fund may occur monthly or at year end, subsequent to receiving the information from the tax collector.

- c. **CAPITAL PROJECTS FUND** - This is a temporary fund, to account for the funds used for the acquisition or construction of major fixed assets. Upon payment, the cost of the asset is transferred from the Capital Projects Fund to the General Fixed Assets Account Group.
- d. **GENERAL FIXED ASSETS ACCOUNT GROUP** - This account group is used to record the cost of fixed assets of the water district. Transfers of the costs constructed assets from the Capital Projects Fund to the General Fixed Assets Account Group are made as payments for the assets are made. Organizational costs, capitalized bond interest, and the cost of fixed assets purchased by other funds should also be accounted for in this fund.
- e. **GENERAL LONG-TERM DEBT ACCOUNT GROUP** - This account group is established to account for the unpaid portion of bonded debt.

4. **Accounting Principles**

The *Governmental Accounting Standards Board* (GASB) has designated the NCGA Statements and Interpretations issued prior to the formation of GASB in 1984 to be the authoritative support for determining GAAP for state and local governments **unless they have been superseded by GASB statements**. Refer to the *Codification of Governmental Accounting and Financial Reporting Standards published by the Governmental Accounting Standards Board* for additional information.

- a. Governmental fund revenues and expenditures should be recognized on the modified accrual basis. Revenues should be recognized in the accounting period in which they become available and measurable. Expenditures should be recognized in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest on general long-term debt, which should be recognized when due. This concept is based on reporting resources and expenditures, not net income.
- b. Proprietary fund revenues and expenditures should be recognized on the accrual basis. Revenues should be recognized in the accounting period in which they are earned and become measurable. Expenses should be recognized in the period incurred, if measurable. Proprietary funds should use commercial accounting principles and terminology.

5. **Governmental Fund Accounting Principles**

- a. **GENERAL FIXED ASSETS** - General fixed assets should be recorded at cost, estimated cost or fair value at the date purchased or contributed to the entity. The cost of fixed assets include its purchase price or construction cost plus all costs necessary to place the asset in service. This includes professional fees and other costs directly related to the installation of facilities. GASB also indicates that the policy regarding capitalization of interest should be disclosed.

- b. **DEPRECIATION OF GENERAL FIXED ASSETS** - It is not appropriate to show depreciation of general fixed assets as an expenditure in the Statement of Revenues, Expenditures and Changes in Fund Balances of a governmental fund. However, accumulated depreciation may be reported in the General Fixed Asset Account Group on the balance sheet.

In contrast, depreciation of fixed assets must be recorded as an expense if enterprise accounting is used.

- c. **PROPERTY TAXES** - Only those property taxes collected within the current period, or soon thereafter (within 60 days), to pay liabilities of the current period should be reported in revenues. The uncollected balance of those property taxes and those collected in advance of the period for which they become available should be reported as deferred revenue.
- d. **INVENTORY OF MATERIALS, SUPPLIES AND PREPAID EXPENDITURES** - A governmental fund entity may report supplies, insurance and other expenditures using the principles applicable to a commercial entity (consumption method) or may report all such amounts as expenditures when acquired (purchase method). Significant amounts of ending inventory should be reported on the balance sheet.
- e. **BOND DISCOUNT** - The *Codification of Governmental Accounting and Financial Reporting Standards* does not address bond discount for a governmental fund. The discount does not have to be recorded as an asset in the General fixed Assets Account Group. However, if the enterprise method of accounting is used, the bond discount must be recognized and amortized over the life of the outstanding bonds.
- f. **DEBT ISSUE PROCEEDS** - The proceeds of long-term debt should be reported as a financing source on the statement of revenues and expenditures. Short-term borrowing should be reported as liabilities in the applicable fund.
- g. **CAPITAL OUTLAY** - Capital outlay includes all costs incurred for construction of facilities and related direct costs which are presumed to benefit both the present and future fiscal periods. This would include:
 - > upgrading facilities,
 - > adding to facilities, and
 - > major overhauls of equipment.

Not all capital outlay expenses are transferred to the General Fixed Assets Fund, only those that are for “general government” purposes. “Specific fund” assets are accounted for in their respective funds.

- h. **RESERVES** - In a governmental fund, accounting and reporting use of the term “reserve” should be limited to indicating that a portion of the fund balance is not available for expenditure or is legally segregated for a specific future use. The reserve for encumbrances should indicate that portion of the fund balance which has been segregated for contractual expenditures such as the unexpended portion of a contract in progress. If part of the fund balance is reserved, the remainder should be reported as designated or unreserved fund balance.

II. ACCOUNTING PROCESS OF A MANUAL OR COMPUTERIZED SYSTEM

Accounting for a governmental entity such as a water district may be done with the use of a computerized or a manual system. Whichever method is chosen, the accounting records should be maintained using GAAP, and the guidelines set forth in this manual. The goal of this manual is not to prescribe rigid accounting procedures, but to establish general guidelines. Some of these guidelines will be discussed in the following section and will be applicable to the records needed in accounting for water districts. See **Appendix J** for a suggested records retention schedule.

A. RECORDS NEEDED

All accounting records described in the *Manual* should be maintained on a fiscal year basis. Various accounting records, journals, registers, and source documents are needed in an accounting system. Basic records used in any accounting system include:

1. Chart of Accounts
2. Special Journals
3. General Journal
4. General Ledger
5. Fixed Asset Register
6. Checkbook
7. Bank Statements
8. Source Documents

1. Chart of Accounts

The Chart of Accounts establishes the capability to classify accounting transactions in a variety of combinations pertinent to the operating and reporting requirements of the district. Any item posted to the district's records will be coded to an account found on the district's Chart of Accounts. An example of a Chart of Accounts with appropriate account descriptions may be found in **Appendix G**.

2. Special Journals

Special journals are used for efficiently recording the transactions which occur frequently. The number of special journals maintained by a district depends on the extent and nature of the district's activities. In computerized systems, the journals may take various forms and may be integrated with the checkbook register (Cash Disbursements Journal). However, in any system, there must be a listing of transactions and accounts to which the transactions were classified, and each transaction must be entered with equal debits and credits. Any such listing can be considered a journal. See **Appendices I & M**.

3. General Journal

The General Journal is also called the "book of original entry." The primary purpose of this journal is to record unique or infrequent transactions that are not appropriately recorded in any of the special journals (including adjusting journal entries).

All entries to the general journal should:

- > classify the transaction by account,
- > appear in chronological order, and
- > include an explanation for the entry with supporting documentation and approval by a responsible person.

4. **General Ledger**

The primary purpose of this ledger is to summarize transactions according to account classifications. Column totals from the journals are computed and transferred to the appropriate accounts in the general ledger. If the governmental accounting method is chosen, the general ledger is organized by fund. All general ledger accounts within a given fund are in account number sequence according to the district's Chart of Accounts.

5. **Fixed Asset Register**

The purpose of this register is to maintain a list of assets purchased/constructed by the district. Each transaction entered in this register should include:

- > the date of the transaction,
- > the source document number and/or description of the transaction, and
- > monetary columns for debits, credits and the total cost of the project.

6. **Checkbook**

A checkbook must be maintained on each checking account. All transactions in the account (cash disbursements, cash receipts, and other transactions) must be recorded in the checkbook. The checkbook should be reconciled at least monthly or at whatever interval the bank statements are received.

7. **Bank Statements**

Bank statements should be received for each bank account maintained. Bank statements may be received monthly, quarterly, or annually depending on the activity in each account. Each statement should be reconciled to the checkbook upon receipt of the statement.

8. **Source Documents**

These are the documents which anticipate an accounting entry to be made. These three types of transaction source documents are discussed in the *Manual*. They are:

- > the cash receipts source document,
- > the cash disbursements source document, and
- > the journal voucher.

The following list typifies the kinds of transaction encountered with source documents.

- a. **CASH RECEIPTS** - These source documents include all cash receipts transactions regardless of their origin. Examples of these transactions include:
 - > service charge receipts
 - > receipts from the sale or redemption of investments,
 - > tap connection fees,
 - > proceeds from the sale of bonds, and
 - > all other cash receipts of the water district.
- b. **CASH DISBURSEMENTS** - These source documents include all cash disbursement transactions. Examples of these transactions include:
 - > debt service payments to the water district's paying agent,
 - > all operating and nonoperating expenditures,
 - > purchases of land and rights-of-way,
 - > improvements to land,
 - > constructing and purchasing fixed assets, and
 - > all other disbursements made by the water district.
- c. **JOURNAL VOUCHERS** - These source documents are used to record all transactions not included in the above two categories. Specifically, they include all adjusting and closing entries and all other transactions not involving cash received or disbursed.

B. CASH TRANSACTIONS

The cash transactions of a General Fund or Enterprise Fund begin with recording the current billing to Revenue and Accounts Receivable accounts. Expenditures are reported to the proper expense account and to the Cash account. The example Chart of Accounts in the **Appendix G** has some of the expense classifications that could be used. The receipts of cash payments are recorded to the Cash and the Accounts Receivable accounts. Also, the receipt should be logged into the Cash Receipts Journal.

The general ledger also provides an important control over transaction entries, as it summarizes all changes in cash. When the cash account is reconciled with the bank statement, there is some assurance that all changes in cash have been classified and recorded in the accounts. In other words, the reconciled cash balance should be the same amount for the account listed in the general ledger.

C. ACCOUNTING FOR OTHER TRANSACTIONS

1. Tap fees

Tap fees should be submitted with a completed tap fee application. The application should contain the following information:

- > description of the lot, block and section,
- > the physical address,
- > the square footage of the lot,

- > the size of the meter,
- > the name of the person requesting the tap, and
- > the amount of the tap fee.

Once this information has been verified, the district should accept payment for the tap and record the receipt in the Tap Fee Journal. In addition to the above information, this journal should also include the check number and the work order number assigned to the tap.

2. **Tax Assessment**

The tax assessment is recorded as Property Tax Revenue and Taxes Receivable at the beginning of the year. A Tax cash account should be set up in the General Fund. The General Fund and the Debt Service Fund each record its proportional share of Taxes Receivable and Property Tax Revenue according to the tax assessment. Tax receipts are debited as Cash in the General Fund when received and the following entries are made:

- > General Fund records a credit to Property Tax Receivable for the operating share of taxes received.
- > The General Fund records the Debt Service portion of taxes received as a credit to Due to the Debt Service Fund.
- > The Debt Service Fund records a credit to Property Tax Receivable for the Debt Service share of taxes received, and a corresponding debit to Due from General Fund.

As Debt Service collections are transferred to the Debt Service Fund the following entries are made:

- > The General Fund records a credit to Cash and a debit to Due to the Debt Service Fund.
- > The Debt Service Fund records a credit to Due from General Fund and a debit to Cash.
- > Uncollected tax receipts are recorded as a credit to Deferred Tax Revenue and a debit to Tax Revenue at year end.

NOTE: **Appendix H** also provides examples of taxes collected by a Tax Fund and by the General and Debt Service Funds individually.

Enterprise Accounting uses the above procedures with a few differences:

- > There is only one combined set of financial statements used for all of the different funds. Thus, no Due to or Due from accounts exist.
- > Depreciation Expense is recorded for all capital assets using a generally accepted method.
- > Bond Interest Expense is accrued over the life of the outstanding bonds, and Organizational Costs are amortized.

D. **FINANCIAL PROCEDURES – ACCOUNTING CONTROLS**

Accounting controls should be incorporated into all phases of the accounting system. The following is an abbreviated list of suggested financial procedures that could be implemented by a district.

1. **Cash Receipts**

Cash is the most liquid of assets and, as such, requires the strictest controls. The use of pre-numbered receipts is considered a standard method of accounting for the receipt of cash. Pre-numbered receipts should contain the following information:

- > customer's name,
- > customer's number,
- > amount of payment,
- > date of payment, and
- > period for which payment is made.

A copy of the receipt should be given to the customer with one copy retained by the clerk receiving the cash and the third copy forwarded to the accounting department.

Payments received in the mail are accounted for in a similar fashion. These payments are usually accompanied by a remittance slip or advice since they are the result of an automated billing system. The same information that is included on a cash receipt should be found on the remittance advice.

Whether the receipt of cash is by mail or in person, the total of all cash receipts and remittance advises should equal the total of cash and checks collected during the day. A reconciliation of receipts to the amount of deposits for the day should also be performed. Lastly, it is important that all checks be restrictively endorsed **“For Deposit Only.”**

2. **Bank Statements**

Bank statements should be reviewed and reconciled by someone other than the person responsible for preparing checks. In addition, it is a good idea for the reconciliation to be reviewed by a third person within the organization.

3. **Journal Entries**

Journal entries should have appropriate backup attached to explain the entry being made and should also be approved by a responsible official.

4. **Invoices**

Invoices received for payment should be reviewed by a responsible official, such as the district manager. Upon approval of the invoice, the official should indicate:

- > the amount to be paid,
- > the date of approval, and
- > the account to be charged.

These approved invoices should then be recorded in the Accounts Payable system and filed in an open invoice file until shortly before the next scheduled board meeting.

During the next board meeting, the invoices should be submitted to the board for approval along with the prepared checks. After the board has approved the invoices and signed the checks, the invoices are stamped "PAID" and the checks are mailed to the payees after making a copy of the check and attaching the copy to the invoice and filing it in the paid invoice file.

5. **Accounts Receivable**

General ledger amounts for accounts receivable should be reconciled to the customer billing ledger each month. Any differences should be investigated and, if appropriate, an adjusting entry should be made to complete the reconciliation.

6. **Customer Deposits**

As with Accounts Receivable, customer deposit accounts should be reconciled to the total of customer deposits recorded in the billing ledger on a monthly basis. Again, any differences noted should be investigated and appropriate action taken.

7. **Tax Collections**

The entry to record tax collections should originate with the report of taxes collected by the tax assessor/collector. It is important that the amounts collected and reported by the tax collector be reconciled with the Taxes Receivable records kept by the district. In this manner, the district can determine the amount and percentage of taxes collected and monitor the time between collection and deposit.

The tax accounts should be separate and distinct from the operating accounts of the district. Care must be taken to avoid a larger than necessary balance from accumulating. At appropriate intervals, amounts should be transferred out of this account and into the Debt Service and operating accounts according to the district's bond requirements and operating procedures.

8. **Budgets**

Perhaps the most effective overall tool used by a district to monitor and control revenues and expenditures is a formally adopted budget. In fact, so much importance has been placed on budgets and budgetary accounting that it is a requirement to formally adopt a budget under current GAAP.

Budgets should be prepared prior to the beginning of a new fiscal year. Budget and accounting line items should be very similar to make comparisons meaningful and easily monitored. A budgeted to actual report, with monthly and year-to-date figures, should be generated monthly and any variances investigated. Material differences that appear permanent usually require an amendment to the existing formal budget.

A formally adopted budget can be a very useful tool for the district. Therefore, it is important that accurate and timely budget reports and other pertinent information be available to the directors on a monthly basis.

III. FINANCIAL REPORTING FOR GOVERNMENTAL UNITS

A. MONTHLY OR QUARTERLY REPORTS TO GOVERNING BOARD

A developed water district's board of directors will usually meet once a month to pay the district's bills and to discuss any important matters. A newly formed district may meet once a month, or once a year, depending upon the district's requirements. The district's board of directors may hire various consultants to perform the duties of the district. Consultants needed by the district may include: a bookkeeper, tax collector, operator, attorney, engineer, financial advisor, and an auditor. In addition, an investment officer must be designated to handle the investment duties of the district as required by the Public Funds Investment Act.

1. Bookkeeper's Responsibilities and Reports

The position of bookkeeper for the district is a more complex job than in the past. The traditional double entry accounting has evolved into a system requiring the use of fund accounting for governments.

Each fund has a particular function and the bookkeeper is responsible for ensuring that all accounts are kept "pure," with no intermingling of monies without the specific direction by the attorney or the Commission.

The bookkeeper is charged with the responsibility of maintaining all records in conformity with this *Manual*. The bookkeeper also is expected to keep the district's funds invested at the highest legal rate of return while remaining insured (when monies are invested, the law specifies securities **MUST** be pledged by the depository to insure the district's investments against any failure of the financial institution). Such activities require constant contact with the investment community to obtain the best rates available.

The district is required to elect a Treasurer of the board. The Treasurer's function is to instruct the bookkeeper in investing district funds appropriately and in accordance with applicable provisions.

Most bookkeepers prepare all checks for approval and signature of the board of directors. Although not authorized to sign checks, bookkeepers can and do transfer funds on behalf of the district. Adequate records must be maintained to enable the auditors to perform yearly audits of all records. This can best be accomplished if all records are kept in accordance with this *Manual* and maintained in such a manner that the auditors have quick and easy access to all records, contracts, minutes of the district meetings, etc.

Other duties of the bookkeeper are: make sure bond payments (due semi-annually) are made in a timely manner; advise the board of any financial problems which may arise due to inadequate or inaccurate rate structures; maintain investment schedules to mature in a timely fashion to meet monthly bills; submit timely revenue and expenditure statements, and to work closely with the attorney, engineer, tax collector, general manager, financial advisor, auditor or other professionals employed by the district.

Most of the accounting records are maintained by the bookkeeper. A revenue and expenditure report for all funds should be prepared by the bookkeeper and submitted for the board's approval at district

meetings. This report should include the past month's ending cash balances for all accounts in each fund, all cash receipts and cash disbursements for the period. The report should reflect the current cash balances. Investments such as money markets and certificates of deposit should be reported. The revenue and expenditure report should balance to the checkbooks and/or the bank statements. Other pertinent information may be requested by the board of directors. Customer deposit liabilities for the period then ended, and information for the next principal and interest payment on bonded indebtedness are examples of information often included in the bookkeeper's report.

All districts are required by the Commission to prepare an annual budget for operating funds utilizing quarterly or monthly budget comparisons. Usually, the bookkeeper will submit a proposed fiscal year budget to the board of directors. The board may or may not make changes to the budget before approval. However, the following year's annual budget must be approved before the close of the current fiscal year. This budget may be amended by the board throughout the fiscal year. **Districts are not required to submit their annual budgets to the Commission, but rather a presentation of actual vs. budgeted costs is required to be included in the annual audit report.**

The bookkeeper may also keep records of all developer reimbursements related to a bond issue. Districts are required to hire an independent auditor to determine the amount to be reimbursed to the developer from the sale of bonds approved by the Commission. The bookkeeper will maintain all copies of invoices and related materials pertaining to developer reimbursements. A comparison report prepared for the board is a useful tool. This report compares the amount of funds approved by the Commission from the bond sale to the actual amount of funds disbursed. In general, capital improvements within the district are performed by the district's developer at the developer's expense. The district is not liable to reimburse the developer for these expenses until the district has sold bonds. Even then, the amount to be reimbursed to the developer is subject to Commission approval. Sometimes a bond sale does not bring in enough money to reimburse the developer the entire amount due to the developer. In these cases, the developer will be reimbursed from a later bond issue.

Other responsibilities of the bookkeeper include:

- > Set up necessary bank accounts, savings accounts, certificates of deposit and other accounts as may be necessary and authorized.
- > Maintain all journals and ledgers pertaining to district funds in accordance with generally accepted accounting principles and this *Manual*.
- > Issue and file 1099's and 1096's at the end of the calendar year.

2. **Tax Assessor/Collector's Responsibilities and Reports**

The comprehensive Texas Property Tax Code, which became effective on January 1, 1982, completely altered the functions of all tax offices. The Property Tax Code was the result of 1979 constitutional amendments and acts of the Texas Legislature.

An explanation of certain provisions of the Tax Code may be found in a book entitled "**Growing by Metes and Bounds**," written by Bob Leared. Contact Bob Leared Interests at 11111 Katy Freeway, Suite 725, Houston, Texas 77079 or phone (713)932-9011.

Generally, a tax collector will calculate and collect the taxes levied by the district. All tax related expenditures will be disbursed by the tax collector. The tax collector must also submit reports to the

board for approval. Each individual tax collector's report varies yet they usually contain approximately the same information. The tax collector's report is important to the district's bookkeeper, since the bookkeeper must post the tax related information to the books from these reports. The bookkeeper generally must rely on information provided by the tax collector. In some instances, the bookkeeper may pay bills and reconcile the bank statements for the tax accounts. See **Appendix M** for a discussion of bank account reconciliation. The tax assessor/collector's report should contain the following information:

- a. TOTAL TAXES LEVIED,
 1. Year,
 2. Rate (debt service and maintenance), and
 3. Levy amount.
- b. AMOUNT OUTSTANDING AT PRESENT,
- c. COLLECTIONS AT PRESENT,
- d. PERCENT COLLECTED,
- e. CURRENT PERIOD REVENUE,
- f. CURRENT PERIOD DISBURSEMENTS (with applicable documentation),
- g. BEGINNING AND ENDING CASH BALANCES,
- h. ACCOUNTS PAYABLE AT YEAR END, and
- i. ANY ADJUSTMENTS TO THE ABOVE LIST.

This report should reflect current period revenues and disbursements. One should also be able to determine the amount of revenues outstanding and collected for the year. At the end of the district's fiscal year, or more often if needed by the board, the tax collector should prepare a delinquent tax roll covering all levy years that have unpaid taxes outstanding.

3. **Operator's Responsibilities and Reports**

The operator's responsibilities parallel those of a city water department. The districts' operator may be responsible for billing and collecting for water, wastewater, and other related services. Examples of the operator's responsibilities may include:

- > meter reading, minimal estimating,
- > routine transfers, turn-ons, turn-offs handled promptly,
- > generation of bills and mailing every 30 days,
- > collection and accounting in accordance with Commission regulations,
- > prompt handling of all customer inquiries,

- > maintenance of all records for audit purposes in accordance with Commission regulations, and
- > enforcement of district's delinquency policy.

All fees billed by the operator are collected by the operator. The operator may deposit these funds directly into the general fund checking account, or a separate collections account may be maintained. In the latter case, all monies collected by the operator are deposited into the collections account. The bookkeeper will then periodically transfer the amount needed to cover expenses to the district's checking account.

Standby fees are usually billed by the operator, but may instead be the bookkeeper's responsibility.

The operator's report is very important to the bookkeeper. The bookkeeper must post all billings and revenue to the books. Since the operator retains all billing and collection records, the bookkeeper must post directly from the operator's report. In order for the bookkeeper to post the operator's records to the books, the reports should contain the following information: (**Appendix L**)

- > Last months receivables - detailed,
- > Current penalties,
- > Any adjustments - detailed,
- > Any write-offs - detailed,
- > Any returned checks,
- > Any other adjustments - detailed,
- > Current payments - detailed,
- > New arrears,
- > Current billing - detailed,
- > Total current receivables - detailed,
- > Deposit liability,
- > Number of connections,
- > Tap fees collected, and
- > Builder damage receivables:
 1. Billed and
 2. Collected.

4. Attorney's Responsibilities and Reports

The attorney for the district performs general legal counsel.

Since districts are strictly regulated, the attorney's assistance is required for obtaining permits, drawing up contracts, annexation procedures, and many other problem-solving duties. He serves as principal negotiator, may handle lawsuits on behalf of the district and keeps current on all laws and regulations.

Every district should have an attorney available to consult with regularly. Good advice solicited on a timely basis can avoid unnecessary complications.

5. Engineer's Responsibilities and Reports

As long as development within the district is active, the engineer should be represented at almost every meeting of the board. When development nears completion, the engineer's activities decrease.

Later, the engineer performs the studies to determine whether expansion of facilities is needed. Along with the attorney and financial advisor, the engineer helps decide when and if additional bond sales would be in the district's best interests.

Also, the engineer makes recommendations regarding new regulations and requirements set forth by the Commission, annexation, outside services, estimated costs, and terms with contractors and sub-contractors.

6. Financial Advisor's Responsibilities and Reports

The following are services in connection with annual operations:

- a. **RECOMMENDATION OF TAX RATE** - The financial advisor meets with the board annually to recommend a tax rate for the succeeding year. It is very important that drastic changes in the district's tax rate be avoided if at all possible. The financial advisor will recommend annual adjustments, if necessary, which will minimize the necessity of dramatic changes in the tax rate. In connection with his recommendation, the financial advisor will present pro forma figures demonstrating the implementation of his tax rate recommendation. Normally, the financial advisor will meet with the district with respect to tax rate recommendations immediately after the tax roll has been established by the district's Appraisal Review Board and certified by its Board of Directors.
- b. **ESTABLISHMENT OF SERVICE RATES** - While the recommendation of rates for water and wastewater service and tap fees is primarily the responsibility of the district's engineer, the financial advisor will review the engineer's recommendations in this regard and provide other information as required by the district.
- c. **DISSEMINATION OF CURRENT FINANCIAL INFORMATION** - The financial advisor will answer requests from investors for current financial information about the district and will compile and distribute such information as required. In the case of a "rated" district, the financial advisor will furnish the rating agency with updated financial data concerning the district on an annual basis.

- d. **OTHER SERVICES** - The financial advisor also performs a variety of other services, such as the review of audit report drafts, the preparation of information reports to be used in connection with bond elections, and assisting the district's board in the dissemination of financial data to residents. The financial advisor can, upon request, be represented at all district meetings where financial matters are to be discussed.

7. Auditor's Responsibilities and Reports

The district is required to conduct an annual audit which must be performed by an independent auditor. Additional work may also be required of an auditor with respect to developer reimbursements for work performed by the developer on the district's behalf.

These are the most common consultants retained by a district. Some districts may require the services of other consultants. The needs of the district will determine the nature and number of consultants used by the district.

8. Investment Officer's Responsibilities and Reports

Each district will designate by rule, order, ordinance, or resolution one or more officers or employees as investment officer that will invest in a manner consistent with the district's adopted investment policy until such authority is rescinded or terminated. The treasurer, or the chief financial officer, and the investment officer of the district will attend at least one training session relating to their responsibilities within twelve months of assuming duty. The training will include education in investment controls, security risks, strategy risks, market risks, and compliance with the Public Funds Investment Act.

Quarterly written reports are required by the Public Funds Investment Act to be provided by the investment officer to the district. They will include these components:

- a. investment position,
- b. preparation by all investment officers,
- c. signature of all investment officers,
- d. summary statement of each pooled fund group,
- e. book and market value of each separately invested asset at the beginning and end of the reporting period by the type of asset and fund type invested,
- f. maturity date of each separately invested asset,
- g. the account or fund or pooled group fund for which each investment was required,
- h. compliance of the investment portfolio as it relates to the investment policy and this act.

B. THE AUDIT

1. Purpose of Financial Reporting

Texas water districts are required by the Texas Water Code to file an independent annual audit report with the Commission unless they meet the criteria to be classified as follows:

- a. **FINANCIALLY DORMANT DISTRICTS** - Districts which can satisfy the criteria in Water Code §49.197(a) may elect to submit a “financial dormancy affidavit” in lieu of an audit.
- b. **DISTRICTS WITH NOMINAL FINANCIAL ACTIVITY** - Districts which can satisfy the criteria in Water Code §49.198(a) may elect to file an “annual financial report” on the Commission’s prescribed forms in lieu of an audit.

The criteria for filing the above reports in lieu of an annual audit report are contained in **Appendix N**, Filing Instructions.

The audit must be performed by a certified public accountant (CPA) or public accountant, licensed by the Texas State Board of Public Accountancy, in accordance with GAAS adopted and promulgated by the American Institute of Certified Public Accountants (AICPA). The Commission has prepared and made available a document entitled Annual Audit Report Requirements (AARR), which discusses a general audit report format, including schedules and other information. The auditor should follow the requirements of the AARR in preparing the annual audit. The AARR also includes more detailed information concerning financial reporting for governmental units.

The audit is an intensive review of the district’s accounting records, systems, and controls which tests a district’s compliance with state law, bond resolutions, and GAAP. The audit involves reviewing district files, contracts, and board meeting minutes to review and verify selected transactions. The auditor must exercise judgement in determining the appropriate auditing procedures to apply. Among other things, the auditor will:

1. Test customer billings for compliance with the district’s rate order;
2. Check whether service billings comply with intergovernmental contracts;
3. Review construction disbursements to determine whether the developer and others have appropriately shared costs;
4. Test the collection of interest earned on investments;
5. Determine whether the district is receiving all appropriate revenues;
6. Examination and analysis of sources of income and disbursements;
7. Analysis of the district’s bonded indebtedness;
8. Determination of accounts receivable and accounts payable;

9. Analysis of the system and controls of the district's consultants as they pertain to functions performed on behalf of the district (**Example:** An analysis of the billings and collections performed by the district's operator or tax assessor/collector);
10. Evaluation of the district's accounting system;
11. Review of the minutes of all board meetings;
12. Review of contracts and agreements entered into by the district;
13. Examination of bond sale proceeds placed in escrow, and determination that the escrowed funds were segregated and on deposit throughout the fiscal period or were disbursed according to the terms prescribed by the Commission or its predecessor; and
14. Compliance with applicable state law (i.e.: Texas Water Code, Local Government Code, etc.).

An audit involves tests of selected types of transactions, physical verification of some types of transactions by the auditor, and written verification of other transactions. Thus, substantial judgement is involved in the determination of the extent and type of procedures to be applied. It is necessary that the auditor question the district's consultants to determine that the accounting records are accurate and properly documented and that all appropriate disclosures have been made.

The CPA is constantly aware that embezzlement can and does occur in the business environment and that is difficult to detect. Audit procedures for the district's annual audit, although they may detect embezzlement, cannot be relied upon for this purpose. Any questionable transaction noted by the auditor should be brought to the board's attention.

In conducting the audit, the auditor will address different interests with varying needs or perspectives. Among the auditor's tasks are the review of records and accounting systems and suggestions for improvements to the board, examination of compliance with bond resolutions, and preparation of the required reports. The auditor also represents the public by reporting on the district's finances and operations. To meet these multiple objectives and best serve his public function, the auditor must maintain his professional independence from the district.

The auditor forms a professional opinion on the district's financial statements. The opinion never states that the financial statements are absolutely accurate. Auditors report on the financial statements as a whole and not on the individual items within the financial statements. The financial statements and other related information presented in the annual report are the representation of the district's board. As a practical matter, the annual report is presented to the board for review before issuing the final report. In the annual report, the auditor reports all questionable transactions to the board. The annual report may form part of the "official statement" used in bond rating applications and for bond sale disclosure material. The district might also distribute its annual report to bond holders and adjacent municipalities.

For financial reporting purposes, GAAP overrides regulatory and statutory requirements. Compliance with financial related legal and contractual provisions should be documented in the supplemental information if it conflicts with GAAP.

2. **The Management Letter**

One of the scope requirements of the audit is that a management letter be prepared by the auditor and presented to the board. The management letter sets forth the auditors' recommendations for improvement to the district's system of internal accounting controls (upon which the scope and extent of audit testing is based); improvement to economy and efficiencies of operations; and improvement to the services provided to customers. The recommendations are required only to the extent that problem areas came to the attention of the auditor during the regular course of the examination.

The directors and consultants should be aware that any remarks made by the auditor in a management letter are intended to be constructive comments, rather than criticism of the past. With a positive attitude, the district can achieve the goal for which it was organized: **to provide quality service to its customers at a reasonable and fair cost.**

3. **The Annual Audit Report**

The annual audit report is the final product of the audit function. The report is comprised of two basic sections: the general purpose financial statements (GPFS) and the supplemental information. The GPFS and the auditor's report are designed to be "liftable" from the report for inclusion in official statements for bond offerings and for widespread distribution to users requiring less detailed information about the district's finances.

The GPFS present the information which is essential to the fair presentation of financial position and results of operations of the district in accordance with GAAP. The supplemental information section contains detailed statistical information and schedules necessary to demonstrate compliance with finance-related, legal and contractual provisions.

4. **Filing Requirements**

Regardless of who prepares the GPFS and Supplemental Schedules, they are the responsibility of the district's governing board. The board is also responsible for assuring the timely filing of the audit report and Annual Filing Affidavit with the Commission, and the audit report in the office of the district as required by law [Water Code §49.194(c)].

Audit reports are to be submitted to the Commission within 135 days after the close of the district's fiscal year [Water Code §49.194(a)]. If the board of the district refuses to approve the annual audit report, the governing board shall submit a copy of the report to the Commission for filing accompanied by a statement from the board explaining the reasons for its failure to approve the report.

Districts with limited or no financial activity may qualify to file an "Annual Financial Report" or "Financial Dormancy and Filing Affidavit" rather than an annual audit report. See **Appendix N** for filing instructions.

C. HOW TO PREPARE FOR THE ANNUAL AUDIT

1. Selecting a Fiscal Year

The board must adopt a fiscal year by a formal resolution within 30 days after the district becomes financially active. The district must notify the Texas Natural Resource Conservation Commission of the adopted fiscal year within 30 days after adoption.

Some of the factors which the directors should consider in the selection of a fiscal year are as follows:

- a. **THE EFFECT ON THE REPORTING OF TAX COLLECTIONS** - If the district assesses taxes on October 1, then the optimum fiscal year-end (so far as this factor is concerned) would be September 30. This allows a full twelve months of collections to be reported in the annual report.
- b. **THE ANTICIPATED DATE OF SALE OF BONDS** - The district's financial advisors may prefer a particular fiscal year in order to facilitate the preparation of the official statement and the sale of bonds.
- c. **THE WORKLOAD OF THE DISTRICT'S AUDITOR** - Since the auditor may have certain months of the year with heavier workloads than others (e.g., tax season), the district may want to set its fiscal year-end at a date which will allow the audit to be performed during the less busy months.
- d. **THE WORKLOAD OF THE DISTRICT'S BOOKKEEPER** - If the district uses a contract bookkeeping service, the directors may want to determine the number of year-end closings which the bookkeeper must complete at the end of each month for its other clients.

Of course, there may be other factors which the board should consider in setting the fiscal year. All of the district's consultants should be contacted to request their input.

2. Selection of an Auditor

As a political subdivision of the State, a district is governed by the Professional Services Procurement Act in selecting an auditor. The Act states, in part, that the district may **NOT** engage the professional services of a CPA selected on the basis of competitive bids submitted for such services. Rather, the Act requires that the district engage a CPA on the basis of demonstrated competence and qualifications for the type of professional services to be performed, and at fair and reasonable prices. The district's other consultants can usually be of help to the directors in locating several CPAs who have demonstrated competence and qualifications in district auditing.

The board should then send requests for proposals to the various CPAs. A suggested format for the requests can be found in **Appendix K**. The requests are designed to ensure that all of the proposals received will be in compliance with the Professional Services Procurement Act, as well as the Rules of Professional Conduct of the Texas State Board of Public Accountancy.

The board should request that each CPA present the written proposal in person at a scheduled board meeting, and be available to answer questions which the directors may have. The personal meeting is helpful to the directors in evaluating how well the CPA will be able to communicate with them on complex financial issues.

It is very important that careful consideration be given to the competency and quality of the CPA selected. The board should engage an auditor with the mutual expectation that he will be serving the district for many years.

3. **Bookkeeper's Preparation for the Audit**

The bookkeeper should compile all information and post the district's books monthly or quarterly. At the end of the district's fiscal year, the bookkeeper should reconcile all ledger accounts and prepare the books for the annual audit. See **Appendix L**.

4. **Audit Preparation Checklist**

a. OPERATING FUND

1. Confirm that prior year accounts payable, accrued interest receivable, any prepaid expense, and prepaid tap accrual entries were properly reversed.
2. Record current year accounts payable, accrued interest, and prepaid expenses.
3. Record deposits applied (if applicable) and clear returned checks.
4. From information provided by operator, record prepaid taps at year end.
5. Verify liability for customer and builder deposits with operator, and record necessary adjustments.
6. Verify cash balances for checking accounts, money market accounts, certificates of deposit, and any other investments.
7. Reconcile accounts receivable to the operator's report.
8. Verify any interfund transfers and due to/from other funds.
9. Verify any amounts due to/from other entities.

After all transactions for the entire fiscal year have been posted, provide the auditor the following:

- > Trial Balance
- > General Ledger
- > Cash Disbursements Journal
- > Cash Receipts Journal
- > General Journal
- > Special Journals

- > Schedule of Accounts Payable
- > Reconciliation of service accounts receivable and standby charges receivable (if applicable) for fiscal year
- > Reconciled bank statements
- > Original invoices with check number and date of payment recorded
- > Investment schedule with copies of applicable documents
- > Source documents for all General Journal entries
- > Budget adopted showing fiscal year end comparison
- > Check stubs/vouchers for the current year
- > Cash receipts for the current year
- > Any correspondence for the fiscal year

b. DEBT SERVICE FUND

1. Confirm that prior year accrued interest amounts have been properly reversed.
2. Record any current year accrued interest.
3. Verify cash balances for checking accounts, money market accounts, certificates of deposit and any other investments.
4. Reverse any prior year accounts payable.
5. Record current year's accounts payable.
6. Record any prepaid interest and/or principal on long-term debt.
7. Verify taxes receivable for current and prior years, and deferred revenue.
8. Verify any interfund transfers and loans to/from other funds.
9. Verify any amounts due to/from other entities.

After all transactions for the entire fiscal year have been posted, provide the auditor the following:

- > Trial Balance
- > General Ledger
- > Cash Disbursements Journal

- > Cash Receipts Journal
- > General Journal
- > Special Journals
- > Schedule of Accounts Payable
- > Reconciled bank statements
- > Original invoices with check number and date of payment recorded
- > Investment schedule with copies of applicable documents
- > Source documents for all journal entries
- > Check stubs/vouchers for the current year
- > Cash receipts for the current year
- > Tax Assessor/Collector reports

c. CAPITAL PROJECTS FUND

1. Confirm that prior year accounts payable, construction contracts payable, and accrued interest receivable accrual entries have been properly removed or reversed.
2. Record current fiscal year accounts payable, construction contracts payable, and accrued interest receivable.
3. Verify cash balances for checking accounts, money market accounts, certificates of deposit and any other investments.
4. Verify any interfund transfers and due to/from other funds.
5. Verify any amounts due to/from other entities.
6. Close work in progress at the end of the fiscal year.

After all transactions for the entire fiscal year have been posted, provide the auditor the following:

- > Trial Balance
- > General Ledger
- > Cash Disbursements Journal
- > Cash Receipts Journal
- > General Journal

- > Special Journals
 - > Reconciled bank statements
 - > Source documents for all General Journal entries
 - > Check stubs/vouchers for the current year
 - > Schedule of Accounts Payable and Construction Contracts Payable
 - > Schedule showing current fiscal year retainage payable
 - > Original invoices with check number and date of payment recorded
 - > Investment schedule with copies of applicable documents
- d. **GENERAL FIXED ASSETS ACCOUNT GROUP** - Verify any interfund transfers from other funds. After all transactions for the entire fiscal year have been posted, provide the auditor the following:
- > Trial Balance
 - > General Ledger
 - > General Journal
 - > Source documents for all general journal entries
- e. **GENERAL LONG-TERM DEBT ACCOUNT GROUP** - Verify long-term balances with the amortization schedule. After all transactions for the entire fiscal year have been posted, provide the auditor the following:
- > Trial Balance
 - > General Ledger
 - > General Journal
 - > Source documents for all General Journal entries
 - > Debt Service amortization schedules for all bond issues

- f. **ADDITIONAL DOCUMENTS TO BE PROVIDED TO THE AUDITOR** - Copies of security ledgers with copies of securities pledged to district at fiscal year end. Copies of any billings by the district.

> Minutes*

> Copies of any agreements entered into by the district, or Commission memos pertaining to the district, such as rate orders adopted during the fiscal year, releases of surplus funds or interest earnings, and escrow releases.*

***NOTE:** These may be obtained from the district's attorney.

5. **After The Audit - Adjusting and Closing Entries**

Once the audit has been completed and approved by the district's board, the auditor should provide the bookkeeper with year-end adjusting and closing entries. There are two methods with which to post the auditor's entries based upon whether the bookkeeper:

- > left all revenue, expense and transfer accounts open; therefore, no entries should have been recorded for the current year (OPEN ACCOUNTS); or
- > closed all revenue, expense, and transfer accounts to the fund balance prior to the audit (CLOSED ACCOUNTS).

6. **Open Accounts**

The adjusting entries should be posted to the appropriate revenue, expense, asset and liability accounts. Then all revenue, expense and transfer accounts should be closed to the appropriate fund balance accounts. After the closing entries have been posted, the balance sheet accounts should be reconciled to the audit report. Current year data can now be posted to the books.

7. **Closed Accounts**

Since all revenue, expense and transfer accounts for the year end have been closed, the auditor's adjusting entries must be modified. All entries posted to an account other than a balance sheet account must be coded to the Fund Balance account. In other words, all entries coded to a revenue, expense or transfer account must be coded to the Fund Balance account. Posting in this manner will adjust appropriate balances to the audit report, and will not affect any current year's information that has been posted.

IV. OTHER TOPICS

A. CASH MANAGEMENT

Regulations - Texas Water Code §49.156 Depository (**Appendix A**), Texas Water Code §49.157 Investments (**Appendix B**), and Vernon's Texas Civil Statutes, Article 842a-2 as amended (**Appendix C**), Vernon's Texas Civil Statutes, Article 2529-b as amended (**Appendix D**), provide the statutory background for the following:

1. **Depository Accounts - (Appendix A)** Generally, a district should have depository accounts as listed below:
 - a. **GENERAL OPERATING ACCOUNT** - receives day-to-day operating receipts and disburses normal operating expenditures. Receipts include revenues from, but not limited to, water, wastewater, maintenance taxes, standby fees, taps, wastewater inspections, interest and any advances from developers. Disbursements include any expenditures related to the normal operations of the district.
 - b. **CAPITAL PROJECTS ACCOUNT** - receives proceeds from bond issues and earnings on investments. Expenditures can be made only in accordance with bond resolutions or, as is the case with surplus funds, as approved by the Commission.
 - c. **TAX ACCOUNT** - receives collections of ad valorem taxes, penalties and interest. Disbursements are made for all costs relevant to the collection of taxes. After collection costs, all funds are transferred to the Debt Service Account or General Operating Account, as appropriate.
 - d. **DEBT SERVICE ACCOUNT** - receives capitalized interest from bond sale and transfers of ad valorem taxes for the purpose of paying the semi-annual bond principal and interest and paying agent fees.
2. **Investment Accounts - (Appendices B and C)** The preservation and safety of the district's principal shall be the primary concern of the board district. To the extent that the principal is protected, district funds shall be invested to yield the highest possible rate of return, taking into consideration the strength of the financial institution and the ability of the financial institution to provide proper security, and complying with any Internal Revenue Code laws or regulations and procedures set forth in any bond resolutions or orders adopted from time to time by the board requiring yield restrictions. Funds of the district shall be invested in accordance with the board's written investment policy.

The board of directors should provide the investment agent authorization to transfer funds to and from the accounts of the district.

- a. **ESCROW AGREEMENTS** - Any funds that must be escrowed by order of the Commission, or other board resolution shall be invested on a basis consistent with the needs of the district. The agreement with the board should stipulate that the original escrow amount can only be released to the district by order or other resolution of the Texas Natural Resource Conservation Commission. The escrowed amount should be so noted on all district financial reports.

- b. **ARBITRAGE** - Federal restrictions on bond proceeds may restrict the yield of investments in the Capital Projects Fund and the Debt Service Fund.
- 3. **Security Requirements - (Appendix D)** all funds shall be insured by the Federal Deposit Insurance Corporation (FDIC) or the Federal Savings and Loan Insurance Corporation (FSLIC) or by collateral pledged to the extent of the fair market value of the amount insured. Funds held in the Debt Service Fund should be handled separately as to security (**Appendix E**). FDIC Regulation #7458 and FSLIC Regulation #5308 both provide for full insurance coverage of an amount up to \$100,000 per bondholder. From a practice standpoint, there could be some difficulties in determining the number of bondholders for a district, therefore, where possible, the investments should be secured in the same manner as the other investments. The amount of funds at any one Texas financial institution will be accumulated to determine the maximum amount of insurance coverage.

To the extent district funds are not insured by the FDIC or FSLIC, there shall be pledged as collateral, to the extent of the market value thereof, any of the securities listed below:

- > obligations of the United States or its agencies and instrumentalities;
- > direct obligations, of the State of Texas or its agencies;
- > other obligations, the principal of interest on which are unconditionally guaranteed or insured by the State of Texas or the United States;
- > obligations of states, agencies, counties cities, and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm and having received a rating of not less than A or its equivalent.

The district shall obtain safekeeping receipts from the Texas financial institution regarding the collateral pledged, and shall determine the fair market value of the collateral pledged at least quarterly. The safekeeping receipt shall describe the security completely, including cusip number when possible. It also should identify the bank making the pledge, the location at which the security is being held and the district which is being secured. See **Appendix A**.

4. **Financial Institutions Reform, Recovery, and Enforcement Act of 1989**

Under FIRREA Section 1823(e), a security agreement, including a pledge of collateral for a deposit, is not valid against the FDIC unless it satisfies the following requirements:

- a. It must be in writing.
- b. It must be executed contemporaneously with the acquisition of the asset by the depository institution.
- c. It must be approved by the depositing institution's board of directors or loan committee, and that approval must be reflected in the minutes of the board or committee.
- d. It must be an official record of the depository institution since it was executed.

If these provisions are not met, the FDIC may be able to avoid a perfected security interest, and the governmental unit only may have the right to share with other creditors in the pro rata distribution of

the assets of a failed institution. Some governmental units may not be in compliance with the requirements listed in (c) above, thereby jeopardizing their deposit collateral.

B. BUDGET PROCESS

1. **Purpose of the Budget** - The operating fund budget should serve as a planning tool. Depending on the development of the district, plans should be implemented to determine the rate of growth of the district, the age of the facilities, possible source of revenue and a method to build a reserve for any unforeseen expenditures. The budget is also used to determine any unforeseen expenditures. The budget can help determine any needed changes in the rate order for water and wastewater services. There are some regulatory requirements which necessitate the use of the budget:
 - a. AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS - requires that a comprehensive operating budget be adopted annually. Codification of Governmental Accounting & Financial Reporting Standards, Section 1700, paragraph 101, "The Budget and Budgetary Accounting".
 - b. TEXAS NATURAL RESOURCE CONSERVATION COMMISSION (**Appendix F**) - requires that an operating budget must be adopted prior to the start of the fiscal year.
2. **Who is Involved in the Budget Process?**
 - a. BOOKKEEPER - should coordinate the preparation of the budget, since he has the prior years' financial information and will ultimately be responsible for providing comparisons.
 - b. ATTORNEY - usually is working with the developer in the development and organization of the district, and has input as to alternate funding methods and any pending elections or litigation.
 - c. ENGINEER - generally has district information from its inception, as well as a knowledge of recommendations for major repairs or future needs.
 - d. OPERATOR - by working in the district on a daily basis, has a knowledge of pending repairs or maintenance of system or any possible modifications.
 - e. TAX COLLECTOR - has knowledge of property values in the district in the event a maintenance tax is required.
 - f. FINANCIAL ADVISOR - needs to know if the operating reserve is adequate for supporting bond ratings; assists in setting the tax rate, if necessary, for a maintenance tax.
 - g. INSURANCE AGENT - can provide information on rate changes or adequacy of coverage of policies.
 - h. OTHER DISTRICTS - some districts have shared facilities and must be appraised of those needs.
 - i. DIRECTORS - provide a continuity of budget knowledge from prior years and are ultimately responsible.

3. **Format of the Budget** - The budget should be customized to fit each district. The board must determine what level of detail is necessary for the planning and monitoring of district operations.

C. **INTERIM REPORTS**

1. **Cash Reports** - they may be presented to board on a monthly basis or whenever the board holds its regular meeting, and should show beginning balances, cash received by all sources, disbursements to be approved, ending balances, and a record of all investments so that the cash position of the district, by fund, can be seen at regular intervals.
2. **Budget Comparisons**- operating fund comparisons may be presented to the board of directors on a quarterly basis, and should indicate actual revenues and expenses as compared to budgeted.
3. **Bond Proceeds Comparison**- at any time bond proceeds are expended, a comparison may be presented to the board of directors to indicate the project items as approved by the Commission, the amounts expended for each item, and difference columns (over or under) of amounts expended to amounts authorized for each item.
4. **Investment Reports**- quarterly written reports are required by the Public Funds Investment Act to be provided by the investment officer to the district. They will include specific components as outlined by the Act (**Appendix C**).

APPENDIX A

Texas Water Code Section 49.156

Depository

- (a) The board, by order or resolution, shall designate one or more banks or savings associations within the state to serve as the depository for the funds of the district. The board shall not be required to advertise or solicit bids in selecting its depositories.
- (b) To the extent that funds in the depository banks or savings associations are not insured by the Federal Deposit Insurance Corporation, they shall be secured in the manner provided by law for the security of funds by Chapter 2257, Government Code (Public Funds Collateral Act).
- (c) The board may authorize a designated representative to supervise the substitution of securities pledged to secure the district's funds.

APPENDIX B

Texas Water Code Section 49.157

Investments

- (a) All district deposits and investments shall be governed by Subchapter A, Chapter 2256, Government Code (Public Funds Investment Act).
- (b) The board may provide that an authorized representative of the district may invest and reinvest the funds of the district and provide for money to be withdrawn from the appropriate accounts of the district for the investments on such terms as the board considers advisable.

APPENDIX C

Government Code Chapter 2256

SECTION 1. Chapter 2256, Government Code, is amended to conform to Section 1, Chapter 181, Section 1, Chapter 858, and Section 1, Chapter 946, Acts of the 73rd Legislature, Regular Session, 1993, and amended to read as follows:

Chapter 2256. Public Funds Investment

Subchapter A. Authorized Investments for Governmental Entities

SEC. 2256.001. SHORT TITLE. This chapter may be cited as the Public Funds Investment Act.

SEC. 2256.002. DEFINITIONS. In this chapter:

- (1) “Bond proceeds” means the proceeds from the sale of bonds, notes, and other obligations issued by an entity, and reserves and funds maintained by an entity for debt service purposes.
- (2) “Book value” means the face or par value of an investment plus accrued interest or minus amortization or accretion.
- (3) “Funds” means public funds in the custody of a state agency or local government that:
 - (A) are not required by law to be deposited in the state treasury; and
 - (B) the investing entity has authority to invest.
- (4) “Institution of higher education” has the meaning assigned by Section 61.003, Education Code.
- (5) “Investing entity” and “entity” mean an entity subject to this chapter and described by Section 2256.003.
- (6) “Investment pool” means an entity created under this code to invest public funds jointly on behalf of the entities that participate in the pool and whose investment objectives in order of priority are:
 - (A) preservation and safety of principal;
 - (B) liquidity; and
 - (C) yield.
- (7) “Local government” means a municipality, a county, a school district, a district or authority created under Section 52(b)(1) or (2), Article III, or Section 59, Article XVI, Texas Constitution, a fresh water supply district, a hospital district, and any political subdivision, authority, public corporation, body politic, or instrumentality of the State of Texas, and any nonprofit corporation acting on behalf of any of those entities.

- (8) “Market value” means the face or par value of an investment multiplied by the premium or discount quoted on the valuation date.
- (9) “Pooled fund group” means an internally created fund of an investing entity in which one or more institutional accounts of the investing entity are invested.
- (10) “School district” means a public school district.
- (11) “Separately invested asset” means an account or fund of a state agency or local government that is not invested in a pooled fund group.
- (12) “State agency” means an office, department, commission, board, or other agency that is part of any branch of state government, an institution of higher education, and any nonprofit corporation acting on behalf of any of those entities.

SEC. 2256.003. AUTHORITY TO INVEST FUNDS; Entities Subject to This Chapter. Each governing body of the following entities may purchase, sell, and invest its funds and funds under its control in investments authorized under this subchapter in compliance with investment policies approved by the governing body and according to the standard of care prescribed by Section 2256.006:

- (1) a local government;
- (2) a state agency
- (3) a nonprofit corporation acting on behalf of a local government or a state agency; or
- (4) an investment pool acting on behalf of two or more local governments, state agencies, or a combination of those entities.

SEC. 2256.004. APPLICABILITY. This subchapter does not apply to:

- (1) a public retirement system as defined by Section 802.001;
- (2) state funds invested as authorized by Section 404.024;
- (3) an institution of higher education having total endowments of at least \$95 million in book value on May 1, 1995; or
- (4) funds invested by the Veterans’ Land Board as authorized by Chapter 161, 162, or 164, Natural Resources Code.

SEC. 2256.005. INVESTMENT POLICIES; INVESTMENT STRATEGIES; INVESTMENT OFFICER.

- (a) The governing body of an investing entity shall adopt by rule, order, ordinance, or resolution, as appropriate, a written investment policy regarding the investment of its funds and funds under its control.

- (b) The investment policies must:
 - (1) be written;
 - (2) primarily emphasize safety of principal and liquidity;
 - (3) address investment diversification, yield, and maturity and the quality and capability of investment management; and
 - (4) include:
 - (A) a list of the types of authorized investments in which the investing entity's funds may be invested;
 - (B) the maximum allowable stated maturity of any individual investment owned by the entity; and
 - (C) for pooled fund groups, the maximum average dollar-weighted maturity allowed based on the stated maturity date for the portfolio.
- (c) The investment policies may provide that bids for certificates of deposit be solicited:
 - (1) orally;
 - (2) in writing;
 - (3) electronically; or
 - (4) in any combination of those methods.
- (d) As an integral part of an investment policy, the governing body shall adopt a separate written investment strategy for each of the funds under its control. Each investment strategy must describe the investment objectives for the particular fund using the following priorities in order of importance:
 - (1) understanding of the suitability of the investment to the financial requirements of the entity;
 - (2) preservation and safety of principal;
 - (3) liquidity;
 - (4) marketability of the investment if the need arises to liquidate the investment before maturity;
 - (5) diversification of the investment portfolio; and
 - (6) yield.
- (e) The governing body of an investing entity shall review its investment policy and investment strategies not less than annually.

- (f) Each investing entity shall designate, by rule, order, ordinance, or resolution, as appropriate, one or more officers or employees of the state agency, local government, or investment pool as investment officer to be responsible for the investment of its funds. Unless otherwise authorized by law, a person may not deposit, withdraw, invest, transfer, or manage in any other manner funds of a state agency, local government, or investment pool without express written authority of the governing body, chief executive officer, or chief financial officer of the state agency, local government, or investment pool, consistent with the investment policy adopted by the entity. Authority granted to a person to deposit, withdraw, invest, transfer, or manage an entity's funds is effective until rescinded by the investing entity or until termination of the person's employment by the investing entity.
- (g) Subsection (f) does not apply to a state agency, local government, or investment pool for which an officer of the entity is assigned by law the function of investing its funds.
- (h) An officer or employee of a commission created under Chapter 391, Local Government Code, is ineligible to be designated as an investment officer under Subsection (f).
- (i) An investment officer of an entity who has a personal business relationship with an entity seeking to sell an investment to the entity shall file a statement disclosing that personal business interest. An investment officer who is related within the second degree by affinity or consanguinity, as determined under Chapter 573, to an individual seeking to sell an investment to the investment officer's entity shall file a statement disclosing that relationship. A statement required under this subsection must be filed with the Texas Ethics Commission and the governing body of the entity.
- (j) The governing body of an investing entity may specify in its investment policy that any investment authorized by this chapter is not suitable.
- (k) A written copy of the investment policy shall be presented to any person seeking to sell to the entity an authorized investment. The registered principal of the business organization seeking to sell an authorized investment shall execute a written instrument substantially to the effect that the registered principal has:
 - (1) received and thoroughly reviewed the investment policy of the entity; and
 - (2) acknowledged that the organization has implemented reasonable procedures and controls in an effort to preclude imprudent investment activities arising out of investment transactions conducted between the entity and the organization.
- (l) The investment officer of an entity may not buy any securities from a person who has not delivered to the entity an instrument in substantially the form provided by Subsection (k).
- (m) An investing entity, in conjunction with its annual financial audit, shall perform a compliance audit of management controls on investments and adherence to the entity's established investment policies. State agencies shall report the results of the audit performed under this subsection to the state auditor. The state auditor shall compile the results of reports received under this subsection and annually report those results to the legislative audit committee.

SEC. 2256.006. STANDARD OF CARE.

- (a) Investments shall be made with judgment and care, under prevailing circumstances, that a person of prudence, discretion, and intelligence would exercise in the management of the person's own affairs,

not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived. Investment of funds shall be governed by the following investment objectives, in order of priority:

- (1) preservation and safety of principal;
 - (2) liquidity; and
 - (3) yield.
- (b) In determining whether an investment officer has exercised prudence with respect to an investment decision, the determination shall be made taking into consideration:
- (1) the investment of all funds, or funds under the entity's control, over which the officer had responsibility rather than a consideration as to the prudence of a single investment; and
 - (2) whether the investment decision was consistent with the written investment policy of the entity.

SEC. 2256.007. Does Not Apply.

SEC. 2256.008. INVESTMENT TRAINING; LOCAL GOVERNMENTS.

- (a) The treasurer, the chief financial officer if the treasurer is not the chief financial officer, and the investment officer of a local government shall attend at least one training session relating to the treasurer's or officer's responsibilities under this chapter within 12 months after taking office or assuming duties.
- (b) Training under this section must include education in investment controls, security risks, strategy risks, market risks, and compliance with this chapter.

SEC. 2256.009. AUTHORIZED INVESTMENTS: OBLIGATIONS OF, OR GUARANTEED BY, GOVERNMENTAL ENTITIES.

- (a) Except as provided by Subsection (b), the following are authorized investments under this subchapter:
 - (1) obligations of the United States or its agencies and instrumentalities;
 - (2) direct obligations of this state or its agencies and instrumentalities;
 - (3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States;
 - (4) other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, this state or the United States or their respective agencies and instrumentalities; and

- (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent.
- (b) The following are not authorized investments under this section:
 - (1) obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal;
 - (2) obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security collateral and bears no interest;
 - (3) collateralized mortgage obligations that have a stated final maturity date of greater than 10 years; and
 - (4) collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

SEC. 2256.010.AUTHORIZED INVESTMENTS: CERTIFICATES OF DEPOSIT. A certificate of deposit is an authorized investment under this subchapter if the certificate of deposit is issued by a state or national bank domiciled in this state or a savings and loan association domiciled in this state and is:

- (1) guaranteed or insured by the Federal Deposit Insurance Corporation or its successor;
- (2) secured by obligations that are described by Section 2256.009(a), including mortgage backed securities directly issued by a federal agency or instrumentality that have a market value of not less than the principal amount of the certificates, but excluding those mortgage backed securities of the nature described by Section 2256.009(b); or
- (3) secured in any other manner and amount provided by law for deposits of the investing entity.

SEC. 2256.011.AUTHORIZED INVESTMENTS: REPURCHASE AGREEMENTS.

- (a) A fully collateralized repurchase agreement is an authorized investment under this subchapter if the repurchase agreement:
 - (1) has a defined termination date;
 - (2) is secured by obligations described by Section 2256.009(a)(1); and
 - (3) requires the securities being purchased by the entity to be pledged to the entity, held in the entity's name, and deposited at the time the investment is made with the entity or with a third party selected and approved by the entity; and
 - (4) is placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in this state.
- (b) In this section, "repurchase agreement" means a simultaneous agreement to buy, hold for a specified time, and sell back at a future date obligations described by Section 2256.009(a)(1), at a market value

at the time the funds are disbursed of not less than the principal amount of the funds disbursed. The term includes a direct security repurchase agreement and a reverse security repurchase agreement.

- (c) Notwithstanding any other law, the term of any reverse security repurchase agreement may not exceed 90 days after the date the reverse security repurchase agreement is delivered.
- (d) Money received by an entity under the terms of a reverse security repurchase agreement shall be used to acquire additional authorized investments, but the term of the authorized investments acquired must mature not later than the expiration date stated in the reverse security repurchase agreement.

SEC. 2256.012.AUTHORIZED INVESTMENTS: BANKERS' ACCEPTANCES. A bankers' acceptance is an authorized investment under this subchapter if the bankers' acceptance:

- (1) as a stated maturity of 270 days or fewer from the date of its issuance;
- (2) will be, in accordance with its terms, liquidated in full at maturity;
- (3) is eligible for collateral for borrowing from a Federal Reserve Bank; and
- (4) is accepted by a bank organized and existing under the laws of the United States or any state, if the short-term obligations of the bank, or of a bank holding company of which the bank is the largest subsidiary, are rated not less than A-1 or P-1 or an equivalent rating by at least one nationally recognized credit rating agency.

SEC. 2256.013.AUTHORIZED INVESTMENTS: COMMERCIAL PAPER. Commercial paper is an authorized investment under this subchapter if the commercial paper:

- (1) has a stated maturity of 270 days or fewer from the date of its issuance; and
- (2) is rated not less than A-1 or P-1 or an equivalent rating by at least:
 - (A) two nationally recognized credit rating agencies; or
 - (B) one nationally recognized credit rating agency and is fully secured by an irrevocable letter of credit issued by a bank organized and existing under the laws of the United States or any state.

SEC. 2256.014.AUTHORIZED INVESTMENTS: MUTUAL FUNDS.

- (a) A no-load money market mutual fund is an authorized investment under this subchapter if the mutual fund:
 - (1) is regulated by the Securities and Exchange Commission;
 - (2) has a dollar-weighted average stated maturity of 90 days or fewer; and
 - (3) includes in its investment objectives the maintenance of a stable net asset value of \$1 for each share.

- (b) In addition to a no-load money market mutual fund permitted as an authorized investment in Subsection (a), a no-load mutual fund is an authorized investment under this subchapter if the mutual fund:
 - (1) is registered with the Securities and Exchange Commission;
 - (2) has an average weighted maturity of less than two years;
 - (3) is invested exclusively in obligations approved by this subchapter;
 - (4) is continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent; and
 - (5) conforms to the requirements set forth in Sections 2256.016(b) and (c) relating to the eligibility of investment pools to receive and invest funds of investing entities.
- (c) An entity is not authorized by this section to:
 - (1) invest in the aggregate more than 80 percent of its monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, in money market mutual funds described in Subsection (a) or mutual funds described in Subsection (b), either separately or collectively;
 - (2) invest in the aggregate more than 15 percent of its monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, in mutual funds described in Subsection (b);
 - (3) invest any portion of bond proceeds, reserves and funds held for debt service, in mutual funds described in Subsection (b); or
 - (4) invest its funds or funds under its control, including bond proceeds and reserves and other funds held for debt service, in any one mutual fund described in Subsection (a) or (b) in an amount that exceeds 10 percent of the total assets of the mutual fund.

SEC. 2256.015.AUTHORIZED INVESTMENTS: GUARANTEED INVESTMENT CONTRACTS.

- (a) A guaranteed investment contract is an authorized investment for state agencies for bond proceeds under this subchapter if the guaranteed investment contract:
 - (1) has a defined termination date;
 - (2) is secured by obligations described by Section 2256.009(a)(1), excluding those obligations described by Section 2256.009(b), in an amount at least equal to the amount of bond proceeds invested under the contract; and
 - (3) is pledged to the entity and deposited with the entity or with a third party selected and approved by the entity.

- (b) Bond proceeds, other than bond proceeds representing reserves and funds maintained for debt service purposes, may not be invested under this subchapter in a guaranteed investment contract with a term of longer than five years from the date of issuance of the bonds.
- (c) To be eligible as an authorized investment:
 - (1) the governing body of the entity must specifically authorize guaranteed investment contracts as an eligible investment in the order, ordinance, or resolution authorizing the issuance of bonds;
 - (2) the entity must receive bids from at least three separate providers with no material financial interest in the bonds from which proceeds were received;
 - (3) the entity must purchase the highest yielding guaranteed investment contract for which a qualifying bid is received;
 - (4) the price of the guaranteed investment contract must take into account the reasonably expected drawdown schedule for the bond proceeds to be invested; and
 - (5) the provider must certify the administrative costs reasonably expected to be paid to third parties in connection with the guaranteed investment contract.

SEC. 2256.016.AUTHORIZED INVESTMENTS: INVESTMENT POOLS.

- (a) An entity may invest its funds and funds under its control through an eligible investment pool if the governing body of the entity by rule, order, ordinance, or resolution, as appropriate, authorizes investment in the particular pool. An investment pool shall invest the funds it receives from entities in authorized investments permitted by this subchapter.
- (b) To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must furnish to the investment officer or other authorized representative of the entity an offering circular or other similar disclosure instrument that contains, at a minimum, the following information:
 - (1) the types of investments in which money is allowed to be invested;
 - (2) the maximum average dollar-weighted maturity allowed, based on the stated maturity date, of the pool;
 - (3) the maximum stated maturity date any investment security within the portfolio has;
 - (4) the objectives of the pool;
 - (5) the size of the pool;
 - (6) the names of the members of the advisory board of the pool and the dates their terms expire;
 - (7) the custodian bank that will safekeep the pool's assets;
 - (8) whether the intent of the pool is to maintain a net asset value of one dollar and the risk of market price fluctuation;

- (9) whether the only source of payment is the assets of the pool at market value or whether there is a secondary source of payment, such as insurance or guarantees, and a description of the secondary source of payment;
 - (10) the name and address of the independent auditor of the pool;
 - (11) the requirements to be satisfied for an entity to deposit funds in and withdraw funds from the pool and any deadlines or other operating policies required for the entity to invest funds in and withdraw funds from the pool; and
 - (12) the performance history of the pool, including yield, average dollar-weighted maturities, and expense ratios.
- (c) To maintain eligibility to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must furnish to the investment officer or other authorized representative of the entity:
- (1) investment transaction confirmations; and
 - (2) a monthly report that contains, at a minimum, the following information:
 - (A) the types and percentage breakdown of securities in which the pool is invested;
 - (B) the current average dollar-weighted maturity, based on the stated maturity date, of the pool;
 - (C) the current percentage of the pool's portfolio in investments that have stated maturities of more than one year;
 - (D) the book value versus the market value of the pool's portfolio, using amortized cost valuation;
 - (E) the size of the pool;
 - (F) the number of participants in the pool;
 - (G) the custodian bank that is safekeeping the assets of the pool;
 - (H) a listing of daily transaction activity of the entity participating in the pool;
 - (I) the yield and expense ratio of the pool;
 - (J) the portfolio managers of the pool; and
 - (K) any changes or addenda to the offering circular.
- (d) An entity by contract may delegate to an investment pool the authority to hold legal title as custodian of investments purchased with its local funds.

- (e) In this section, “yield” shall be calculated in accordance with regulations governing the registration of open-end management investment companies under the Investment Company Act of 1940, as promulgated from time to time by the federal Securities and Exchange Commission.

SEC. 2256.017.PORTFOLIO OF CERTAIN INVESTMENT POOLS.

A public funds investment pool created to function as a money market mutual fund must mark its portfolio to market daily and, to the extent reasonably possible, stabilize at a \$1 net asset value. If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, portfolio holdings shall be sold as necessary to maintain the ratio between 0.995 and 1.005.

SEC. 2256.018.ADVISORY BOARD OF INVESTMENT POOLS.

- (a) An investment pool other than a pool described by Subsection (b) shall establish an advisory board composed of participants in the pool and other persons.
- (b) A public funds investment pool created under Chapter 791 and managed by a state agency shall establish an advisory board composed equally of participants in the pool and other persons who do not have a business relationship with the pool. A board member must be qualified to advise the pool.

SEC. 2256.019.RATING OF CERTAIN INVESTMENT POOLS.

A public funds investment pool must be continuously rated no lower than AAA or AAA-m or at an equivalent rating by at least one nationally recognized rating service.

SEC. 2256.020.Does Not Apply.

SEC. 2256.021.EFFECT OF LOSS OF REQUIRED RATING.

An investment that requires a minimum rating under this subchapter does not qualify as an authorized investment during the period the investment does not have the minimum rating. An entity shall take all prudent measures that are consistent with its investment policy to liquidate an investment that does not have the minimum rating.

SEC. 2256.022.EXPANSION OF INVESTMENT AUTHORITY.

Expansion of investment authority granted by this chapter shall require a risk assessment by the state auditor or performed at the direction of the state auditor.

SEC. 2256.023.INTERNAL MANAGEMENT REPORTS.

- (a) Not less than quarterly, the investment officer shall prepare and submit to the governing body of the entity a written report of investment transactions for all funds covered by this chapter for the preceding reporting period.
- (b) The report must:
 - (1) describe in detail the investment position of the entity on the date of the report;
 - (2) be prepared jointly by all investment officers of the entity;

- (3) be signed by each investment officer of the entity;
- (4) contain a summary statement of each pooled fund group that states the:
 - (A) beginning market value for the reporting period;
 - (B) additions and changes to the market value during the period; and
 - (C) ending market value for the period;
- (5) state the book value and market value of each separately invested asset at the beginning and end of the reporting period by the type of asset and fund type invested;
- (6) state the maturity date of each separately invested asset that has a maturity date;
- (7) state the account or fund or pooled group fund in the state agency or local government for which each individual investment was acquired; and
- (8) state the compliance of the investment portfolio of the state agency or local government as it relates to:
 - (A) the investment strategy expressed in the agency's or local government's investment policy; and
 - (B) relevant provisions of this chapter.
- (c) The report shall be presented not less than quarterly to the governing body and the chief executive officer of the entity within a reasonable time after the end of the period.

SEC. 2256.024.SUBCHAPTER CUMULATIVE.

- (a) The authority granted by this subchapter is in addition to that granted by other law. Except as provided by Subsection (b), this subchapter does not:
 - (1) prohibit an investment specifically authorized by other law; or
 - (2) authorize an investment specifically prohibited by other law.
- (b) Except with respect to those investing entities described in Subsection (c), a security described in Section 2256.009(b) is not an authorized investment for a state agency, a local government, or another investing entity, notwithstanding any other provision of this chapter or other law to the contrary.
- (c) Mortgage pass-through certificates and individual mortgage loans that may constitute an investment described in Section 2256.009(b) are authorized investments with respect to the housing bond programs operated by:
 - (1) the Texas Department of Housing and Community Affairs or a nonprofit corporation created to act on its behalf;
 - (2) an entity created under Chapter 392, Local Government Code; or

- (3) an entity created under Chapter 394, Local Government Code.

Subchapter B. Miscellaneous Provisions

SEC. 2256.051. ELECTRONIC FUNDS TRANSFER.

Any local government may use electronic means to transfer or invest all funds collected or controlled by the local government.

SEC. 2256.052 THROUGH 2256.055. Does Not Apply.

SECTION 2. Does Not Apply.

SECTION 3. Does Not Apply.

SECTION 4. Does Not Apply.

SECTION 5. Section 1, Chapter 181; Section 1, Chapter 858; and Section 1, Chapter 946, Acts of the 73rd Legislature, Regular Session, 1993, are repealed.

SECTION 6. As provided by Section 1.02, Senate Bill No. 959, Acts of the 74th Legislature, Regular Session, 1995, this Act controls over Senate Bill No. 959 to the extent of any conflict.

SECTION 7. Each member of a governing board and each investment officer who is in office or who has assumed duties on September 1, 1995, and who would be required by Section 2256.007(a), Government Code, as amended by this Act, to attend investment training within six months after taking office or assuming duties shall attend at least one training session relating to the person's responsibilities under Chapter 2256, Government Code, that meets the requirements of that section not later than March 1, 1996.

SECTION 8. Each treasurer, chief financial officer, and investment officer who is in office or who has assumed duties on September 1, 1995, and who would be required by Section 2256.008(a), Government Code, as amended by this Act, to attend investment training within 12 months after taking office or assuming duties shall attend at least one training session relating to the person's responsibilities under Chapter 2256, Government Code, that meets the requirements of that section not later than September 1, 1997.

SECTION 9. The state auditor shall conduct, or shall hire an independent evaluator to conduct, an assessment of the risks and benefits associated with authorizing entities subject to this chapter to invest in mutual funds other than money market mutual funds, investment pools other than investment pools that function as money market mutual funds, and guaranteed investment contracts. The state auditor shall report these findings to the legislature not later than September 1, 1996. This section expires on September 2, 1996.

SECTION 10. This Act takes effect September 1, 1995.

SECTION 11. An entity that acquired authorized investment securities under Chapter 2256, Government Code, before the effective date of this Act that are no longer authorized investment securities under that chapter as amended by this Act is not required by this Act to liquidate those securities before the final stated maturity of the investment.

SECTION 12. The importance of this legislation and the crowded condition of the calendars in both houses create an emergency and an imperative public necessity that the constitutional rule requiring bills to be read on three several days in each house be suspended, and this rule is hereby suspended.

APPENDIX D

Vernon's Texas Civil Statutes Article 2529(d), as amended

SECTION 1. SHORT TITLE. This Act may be cited as the Public Funds Collateral Act.

SECTION 2. DEFINITIONS. In this Act:

- (1) "Board" means the State Depository Board.
- (2) "Control" and "bank holding company" have the same meanings assigned by Article 2, Chapter I, The Texas Banking Code (Article 342-102, Vernon's Texas Civil Statutes).
- (3) "Deposits of public funds" means public funds of a public entity that:
 - (A) are not managed by the state treasurer under Chapter 404, Government Code; and
 - (B) are held as a demand or time deposit at a bank or other depository institution expressly authorized by law to accept demand or time deposits of the public entity.
- (4) "Eligible security" means:
 - (A) surety bonds;
 - (B) investment securities; and
 - (C) ownership or beneficial interests in investment securities but not any option contract to purchase or sell investment securities.
- (5) "Exempt institution" means:
 - (A) a public retirement system, as defined by Section 802.001, Government Code; and
 - (B) the permanent school fund, as defined by Section 15.01, Education Code.
- (6) "Investment security" means:
 - (A) a direct obligation of the United States;
 - (B) an obligation that in the opinion of the Attorney General of the United States is a general obligation of the United States and backed by its full faith and credit;
 - (C) an obligation, the principal of and interest on which are unconditionally guaranteed by the United States;

- (D) an obligation of an agency or instrumentality of the United States, including a mortgage-backed security of the agency or instrumentality;
 - (E) a general or special obligation issued by a public agency, payable from taxes, revenues, or a combination of taxes and revenues that has been rated as to investment quality by a nationally recognized rating agency and that has a current rating of not less than A or its equivalent; and
 - (F) any security in which a public entity may invest under the Public Funds Investment Act of 1987 (Article 842a-2, Vernon's Texas Civil Statutes).
- (7) "Permitted institution" means:
- (A) a Federal Reserve Bank;
 - (B) a "clearing corporation" as defined in Subsection (c), Section 8.102, Business & Commerce Code;
 - (C) any bank eligible to be a custodian under Subsection (c) of Section 6 of this Act; and
 - (D) any state or nationally chartered bank, which bank is controlled by a bank holding company that controls a bank eligible to be a custodian under Subsection (c) of Section 6 of this Act.
- (8) "Public agency" means any state or any political or governmental entity, agency, instrumentality, or subdivision of a state, including without limitation municipalities, state-supported educational institutions, junior colleges, districts established pursuant to Article XVI, Section 59, of the Texas Constitution, and public hospitals.
- (9) "Public entity" means any public agency in this state that is not an institution of higher education as defined by Section 61.003, Education Code.
- (10) "State agency" means a public entity that:
- (A) has authority that is not limited to a geographic portion of the state; and
 - (B) was created by constitution or a statute of this state.
- (11) "Trust receipt" means evidence of receipt, identification, and recording, including but not limited to physical controlled trust receipt or written or electronically transmitted advice of transaction.

SECTION 3. AUTHORIZED COLLATERAL. Deposits of public funds shall be secured by eligible security to the extent and in the manner required by this Act.

SECTION 4. LEVEL OF COLLATERAL. The total of the face value of the surety bonds and the market value of the investment securities securing the deposits of public funds shall be in an amount at least equal to the amount of the deposits of public funds increased by the amount of any accrued interest and reduced to the extent that the deposits are insured by an agency or instrumentality of the United States government.

SECTION 5. COLLATERAL POLICY; PUBLIC ENTITY CONTRACTS.

- (a) Investment securities eligible to secure deposits of public funds shall be determined in accordance with written policies approved by the governing body of the public entity. The written policies may address matters including security of the institution obtaining or holding investment securities, substitution or release of investment securities, and the method of valuation of investment securities used to secure deposits of public funds.
- (b) A public entity may contract with a bank domiciled in this state to determine the terms and conditions for securing deposits of public funds. The contract may contain terms and conditions relating to the investment securities used as security for deposit of public funds that are acceptance to the public entity, including provisions relating to the possession of the collateral, the substitution or release of investment securities, the ownership of the investment securities of the bank used to secure deposits of public funds, and the method of valuation of investment securities used to secure deposits of public funds.
- (c) The public entity shall inform the depository of its deposits of public funds of significant changes in the amount or activity of deposits of public funds reasonable in advance of such changes.

SECTION 6. POSSESSION OF COLLATERAL.

- (a) In addition to all other authority granted by law, a depository for any public entity may deposit the securities pledged to secure deposits of public funds with a custodian as provided in this Act. At the request of the public entity, the depository shall place the pledged securities with a custodian as provided in Subsection (c) of this section. The public entity may require that the depository not be the custodian or permitted institution or a branch of either with respect to the particular securities pledged by the depository to secure deposits of public funds.
- (b) Notwithstanding Subsection (a) of this section, the depository of deposits of public funds for any state agency shall place the pledged securities with a custodian as provided in Subsection (c) of this section. The custodian and the state agency shall execute a written agreement to determine the terms and conditions for securing deposits of public funds. The depository for a state agency shall not be the custodian or permitted institution or a branch of either with respect to the particular securities pledged by the depository to secure deposits of public funds.
- (c)
 - (1) A depository for a public entity may deposit investment securities pledged to secure deposits of public funds with a custodian that the public entity has approved as a custodian and that is either:
 - (A) a state or national bank which is domiciled within this state, which has been designated a state depository by the board, and which has a capital stock and permanent surplus of not less than \$5 million;
 - (B) the Texas Treasury Safekeeping Trust Company; or
 - (C) a Federal Reserve Bank or its branches.
 - (2) The securities shall be held in trust by the custodian to secure the deposits of public funds of the public entity in the depository pledging the securities.

- (d) On receipt of the investment securities, the custodian shall immediately, by book entry or otherwise, identify on its books and records the pledge of the securities to the public entity and shall promptly issue and deliver to the appropriate official of the public entity trust receipts for the securities pledged. The security evidenced by the trust receipts is subject to inspection by the public agency or its agents at any time.
- (e) A custodian holding in trust investment securities of a depository under Subsection (c) of this section may deposit the pledged securities with a permitted institution. The securities shall be held by the permitted institution to secure funds deposited by the public entity in the depository pledging the securities. On receipt of the securities, the permitted institution shall immediately issue to the custodian an advice of transaction or other document evidencing the deposit of the securities. When the pledged securities held by a custodian are deposited, the permitted institution may apply book entry procedures to the securities. The records of the permitted institution shall at all times reflect the name of the custodian depositing the pledged securities. The trust receipts the custodian issues to the public entity shall indicate that the custodian has deposited with the permitted institution the pledged securities held in trust for the depository pledging the securities.

SECTION 7. VENUE. Any legal action or proceeding by or against the public entity, arising out of or in connection with the duties of the depository, the custodian, or a permitted institution under this Act, shall be brought and maintained as provided in the contract with the public entity.

SECTION 8. PRIORITY. Any custodian under this Act and any custodian of securities pledged to an institution of higher education as defined by Section 61.003, Education Code, acting alone or through a permitted institution, shall for all purposes under state law, notwithstanding anything in Chapters 8 and 9 of the Business & Commerce Code to the contrary, be the bailee or agent of the public entity or institution depositing such public funds with the depository, and the security interest arising out of a pledge of securities to secure deposits of the public entity or institution shall be created, shall attach, and shall be perfected for all purposes under state law from the time that the custodian identifies the pledge of the securities on its books and records and issues the trust receipts and remains as of that time perfected in the hands of all subsequent custodians and permitted institutions.

SECTION 9. RECORDS; REPORTS.

- (a) The depository for a public entity shall maintain separate, accurate, and complete records relating to all deposits of public funds, the pledged investment securities, and all transactions relating to the pledged investment securities.
- (b) The custodian for a public entity shall maintain separate, accurate, and complete records relating to the pledged investment securities and all transaction relating to the pledged investment securities.
- (c) The board or the public entity may examine and verify at any reasonable time all pledged investment securities and all records maintained pursuant to Subsections (a) and (b) of this section.
- (d) As a part of each internal or external audit or regulatory examination of the depository for a public entity and of the custodian for a public entity, the auditor or examiner shall examine and verify the pledged investment securities and the records maintained pursuant to Subsections (a) and (b) of this section and shall report any significant or material noncompliance with the provisions of this Act to the board.
- (e) The custodian for the public entity shall file a collateral report with the board in the manner and on the dates prescribed by the board.

SECTION 10. PENALTIES.

- (a) The board may revoke a designation as a state depository if, after notice and a hearing, the board makes a written finding that the depository, acting in its capacity either as a depository or a custodian, as the case may be, does not maintain reasonable compliance with this Act and has failed to remedy any violation of this Act within a reasonable period of time after written notice of such violation. Such revocation shall be effective for a period of one year.
- (b) If the board makes a written finding that the depository has not maintained reasonable compliance with this Act and has acted in bad faith in not remedying any violations of this Act, the board may permanently revoke the designation as a state depository.
- (c) If the board determines that the depository has remedied all violations of this Act and has given assurances satisfactory to the board that the depository will maintain reasonable compliance with this Act, the board may reinstate its designation as a state depository.
- (d) When making the findings required by Subsection (a) or (b) of this section, the board shall consider the totality of the circumstances regarding the performance of the depository or the custodian, including but not limited to the extent to which the noncompliance with this Act is minor, isolated, temporary, or nonrecurrent. The board shall not find that either the depository or the custodian does not maintain reasonable compliance with this Act if such noncompliance is a result of the failure of the public entity to comply with Subsection (c) of Section 5 of this Act.
- (e) Subsection (d) of this section shall not relieve the depository or the custodian of the obligation to secure deposits of public funds with eligible security in the amount and manner required by this Act within a reasonable time after the public entity deposits and deposits of public funds with the depository.

SECTION 11. ACT CONTROLLING.

- (a) To the extent of any conflict between this Act and another law relating to security for deposits of public funds, this Act prevails.
- (b) An exempt institution is not required to have its funds at all times fully insured or collateralized if such funds are held by a custodian of its assets pursuant to a trust agreement or held by an entity in connection with investment-related transactions and if, in the exercise of its fiduciary responsibilities, the governing body of the exempt institution determines that the exempt institution is adequately protected through the use of trust agreements, special deposits, surety bonds, substantial deposit insurance, or any other method commonly used by such institutions. This Act does not prohibit prudent investment by the exempt institution in certificates of deposit or restrict the selection of depositories by the governing body of the exempt institution in accordance with its fiduciary duties.
- (c) This Act does not apply to funds maintained and administered by a public entity pursuant to a deferred compensation plan the federal income tax treatment of which is governed by Section 401 or 457 of the Internal Revenue Code of 1986.

NOTE: A security agreement, including a pledge of collateral for a deposit, may not be valid against the FDIC under certain conditions. See Section IV A., 4.

APPENDIX E

FDIC Regulation 7458

- (b) Public bond issues. Where an officer, agent or employee of a public unit has custody of certain funds which by law or under the bond indenture are required to be paid to the holders of bonds issued by the public unit, any deposit of such funds in an insured bank shall be deemed to be a deposit by a trustee of trust funds of which the bondholders are pro rata beneficiaries, and each such beneficial interest shall be separately insured up to \$100,000.

FSLIC Regulation 5308

- (b) Public bond issues. Where an officer, agent or employee of a public unit has custody of certain funds which by law or under the bond indenture are required to be paid to the holders of bonds issued by the public unit, any investment of such funds in an insured institution shall be deemed to be an investment by a trustee or trust funds of which the bondholders are pro rata beneficiaries, and each such beneficial interest shall be separately insured up to \$100,000.

APPENDIX F

30 Texas Administrative Code Paragraph 293.97 (Rules of the Texas Natural Resource Conservation Commission)

- “(b) **Operating Budget.** Prior to the start of a fiscal year, the governing board of each district shall adopt an operating budget for the upcoming fiscal year. The adopted budget and any subsequent amendments shall be passed and approved by a resolution of the governing board minutes. Budget amendments are required by the commission only if events occur which prevent meaningful comparison of the budget to the actual results of operation. The adopted budget is not a spending limitation imposed by the commission. However, the governing board may adopt rules to limit the spending authority of the district officers in relation to the budget. A comparison of the actual operating results to the adopted budget, as amended, shall be presented in the annual report of each district. The budgetary comparison statement shall be included either within the audited financial statements or within a supplementary section.”

APPENDIX G

Sample Chart of Accounts

GENERAL LONG-TERM DEBT ACCOUNT GROUP			
	Assets		
1500	To be Provided for Bonded Debt	1411	Organizational Costs - Interest on Temporary Investments
		1413	Organizational Costs - Election Costs
		1415	Organizational Costs - Other Costs
		1417	Organizational Costs - Interest on Purchase of Facilities
	Liabilities		Fund Balance
2510	Bonds Payable, Series _____	3001	Investment in Fixed Assets -From Net System Revenues
2511	Bonds Payable, Series _____	3009	Investment in Fixed Assets - From Investment Revenues
2512	Bonds Payable, Series _____	3010	Investment in Fixed Assets - From Sale of Bonds
2513	Bonds Payable, Series _____	3011	Investment in Fixed Assets - Contributed by Developer
2514	Bonds Payable, Series _____	3013	Investment in Fixed Assets - Contributed by Other Districts
2515	Bonds Payable, Series _____	3014	Investment in Fixed Assets - Contributed by Governmental Agency
GENERAL FIXED ASSET ACCOUNT GROUP			
	Assets		
1310	Land, Easements and Right-of-Ways		
1311	Buildings		
1312	Water System		
1313	Sewage System		
1314	Drainage System		
1315	Machinery and Equipment	1110	Cash - Capital Projects (establish multiple accounts if different bank accounts used; i.e., 1122, 1123...)
1316	Automobiles and Trucks	1122	Cash in Escrow
1317	Furniture and Fixtures	1140	Time Deposits for Construction Projects (includes certificates of deposit, savings certificates and saving accounts - details provided by schedule)
1318	Engineering Fees		
1351	Construction in Progress, _____ Bond Issue	1141	Certificates of Deposit for Construction Projects
1352	Construction in Progress, _____ Bond Issue	1158	Accrued Investment Interest Receivable
1353	Construction in Progress, _____ Bond Issue	1160	Prepaid Tap Expense
1354	Construction in Progress, _____ Bond Issue	1171	Due from General Fund
1401	Organizational Costs - Legal Fees	1176	Due from Other Districts
1403	Organizational Costs - Bond Interest	1177	Due from Developer - Currently Due
1407	Organizational Costs - Fiscal Agent Fees	1178	Due from Developer - Deferred (Retainage)
1409	Organizational Costs - Bond Interest Expenses		

CAPITAL PROJECTS FUND

Assets

Sample Chart of Accounts – Continued

CAPITAL PROJECTS FUND – Continued		Other Additions to Reserves	
Liabilities		3955	Proceeds from Sale of Bonds
		3956	Developer Contributions
2110	Trade Accounts Payable	3957	Governmental Agency Contributions
2119	Accrued Interest Payable	3958	Other Districts' Contributions
2120	Short-Term Notes Payable	3959	Bond Anticipation Note Proceeds
2125	Due to Other Districts	3960	Sale of Fixed Assets
2126	Due to Developer	3961	R.W.T.P. Rebate
2130	Construction Contracts Payable		
2140	Construction Contracts Payable - Retained Percentage		Revenues
2150	Bond Anticipation Notes Payable	5380	Miscellaneous Income
2171	Due to General Fund	5391	Interest on Temporary Investments
Fund Balance			Expenses
3000	Unreserved Fund Balance	7300	Capital Outlay, _____ Bond Issue
	(Construction fund interest not required to be transferred)	7301	Capital Outlay, _____ Bond Issue
3001	Reserved - From Net System Revenues	7302	Capital Outlay, _____ Bond Issue
3003	Interest Earnings Not Transferred	7303	Capital Outlay, _____ Bond Issue
3010	Reserved - From Sale of Bonds for Authorized Construction, Prior Issues (Prior Issues added to title)	7304	Capital Outlay, _____ Bond Issue
		7305	Capital Outlay, _____ Bond Issue
		7362	Interest Expense on Notes
3011	Reserved - From Sale of Bonds for Authorized Construction, _____ Issue	7395	Other Expense
3012	Reserved - From Sale of Bonds for Authorized Construction, _____ Issue		GENERAL FUND
3013	Reserved - From Sale of Bonds for Authorized Construction, _____ Issue		Assets
3014	Reserved - From Sale of Bonds for Authorized Construction, _____ Issue	1110	Cash (establish multiple accounts if different bank accounts used i.e., 1110, 1111, _____)
3015	Reserved - From Sale of Bonds for Authorized Construction, _____ Issue	1122	Cash in Banks for Meter Deposits
		1130	Time Deposits (includes certificates of deposit, savings certificate and savings accounts - details provided by schedule)
Fund Transfers			
3911	Transferred to General Fund	1131	Certificates of Deposits
3913	Transferred to Debt Service Fund	1145	Service Accounts Receivable
3951	Transferred from General Fund	1146	Allowance for Uncollectible Service Accounts
3953	Transferred from Debt Service Fund	1147	Service Account Interest Receivable (included in account #1145)

Sample Chart of Accounts – Continued

GENERAL FUND – Continued		2701	Tap Connections Fees - Advance Payments (Deferred water and sewer tap fees)
Assets – Continued		2702	Sewer Tap Connection Fees - Advance Payments
1148	Service Account Penalties Receivable (included in account #1145)	2740	Deferred Revenues - Uncollected Taxes
1149	Returned Checks	2750	Deferred Revenues - Uncollected Standby Charges
1150	Taxes Receivable		
1155	Builder Damages Receivable		
1156	Accounts Receivable - Other		
1157	Standby Charges Receivable		
1158	Accrued Investment Interest Receivable		
1159	Tap Fees Receivable	3000	Unreserved Fund Balance
1160	Prepaid Tap Expense	3002	Allocated from Net Tax Revenues
1161	Prepaid Insurance	3005	Reserved for Operating Expenses
1172	Due from Tax Fund	3007	Investment in Inventories
1173	Due from Debt Service Fund	3913	Transferred to Debt Service Fund
1174	Due from Capital Projects Fund	3914	Transferred to Capital Projects Fund
1176	Due from Other Districts	3952	Transferred from Tax Fund
1190	Material and Supplies	3953	Transferred from Debt Service Fund
1191	Meters	3954	Transferred from Capital Projects Fund
		3960	Sale of Fixed Assets
Liabilities			
2110	Trade Accounts Payable		
2111	Salaries and Wages Payable	4100	Customer Service Fees - Water
2112	OASI Taxes Payable	4101	Bulk Water Sales
2113	Withholding Taxes Payable	4102	Water Service Inspection Fees
2114	Employee Retirement Premiums Payable	4103	Service Fees - Other Governmental Units
2115	Group Insurance Premiums Payable	4110	Water Tap Connection Fees
2119	Accrued Interest Payable	4120	Reconnection Fees
2120	Short-Term Notes Payable		
2125	Due to Other Districts		
2130	Professional Fees Payable (combined with account #2110)		
2161	Customer Meter Deposits Payable	4200	Customer Service Fees - Sewer
2173	Due to Debt Service Fund	4202	Service Inspection Fees
2174	Due to Capital Projects Fund	4203	Service Fees - Other Governmental Units
2251	Sewer Deposits Payable	4210	Sewer Tap Connection Fees
2552	Advance from Tax Fund		
2554	Advance from Capital Projects Fund		

Sample Chart of Accounts – Continued

GENERAL FUND – Continued		6155	Uncollectible Accounts
Revenues: Other		6157	Rents and Leases - Equipment
4320	Property Taxes	6158	Rents and Leases - Space
4330	Penalties & Interest on Service Accounts	6160	Damage Claims (Credit Account)
4331	Penalties & Interest on Tax Accounts	6161	Garbage Collection Expense
4400	Collection Agency Income	6170	Tap Connection - Materials and Labor
4500	Standby Charges	6171	Tap Connection - Contract
4501	Sewer Availability Charges	6180	Reconnection Expense
4600	Tap Connection Fees		Sewer Service Expenses
5380	Miscellaneous Income	6201	Purchased Sewer Services
5390	Deposits Forfeited	6211	Salaries and Wages
5391	Interest on Temporary Investments	6212	Employee Retirement Premiums
5392	Gain on Sale of Investments	6213	Group Insurance Premiums
5395	Sale of Fixed Assets	6214	Employers FICA Tax Expense
5396	Rental and Lease Income	6215	Workmen's Compensation Premiums
	Water Service Expenses	6223	Management of STP facilities
6100	Bulk Water Purchase	6234	Contract Labor
6111	Salaries and Wages	6235	Maintenance and Repairs
6112	Employee Retirement Premiums	6241	Fuel and Lubricants
6113	Group Insurance Premiums	6242	Chemicals
6114	Employers OASI Tax Expense	6244	Repair and Maintenance - Materials
6115	Workmen's Compensation Premiums	6246	Materials Applied to Tap Connection Expense
6116	Labor Applied to Tap Connection Expense	6249	Other Consumable Supplies and Materials
6134	Contract Labor	6250	Postage
6135	Maintenance and Repairs	6253	Insurance
6136	Meter Installation	6255	Uncollectible Accounts
6137	Meter Reading	6257	Rents and Leases - Equipment
6138	Legal Notices and Other Publications	6259	Other Expense
6141	Fuel and Lubricants	6260	Damage Claims (Credit Account)
6142	Chemicals	6270	Tap Connection - Materials and Labor
6143	Small Tools	6271	Tap Connection - Contract
6144	Repair and Maintenance - Materials	6275	Sewer Inspection Expense
6145	Meter Expenses	6285	Costs Reimbursed by Other Districts
6146	Materials Applied to Tap Connection Expense		Other Operating Expenses
6149	Other Consumable Supplies and Materials	6310	Director Fees
6150	Postage	6311	Salaries and Wages
6153	Insurance	6312	Employee Retirement Premiums
		6313	Group Insurance Premiums
		6314	Employers OASI Tax Expense

Sample Chart of Accounts – Continued

6315	Workmens' Compensation Premiums	1152	Tax Account Interest Receivable
6320	Legal Fees	1153	Tax Account Penalties Receivable
6321	Auditing Fees	1158	Accrued Investment Interest Receivable
6322	Engineering Fees		
6323	Management and Consulting	1160	Allowance for Uncollectible Taxes
6324	Laboratory Expenses	1171	Due from General Fund
6325	Election Expense	1173	Due from Debt Service Fund
6326	Permit Fees		
6332	Service Account Collection		Liabilities
6333	Bookkeeping		
6334	Contract Labor	2110	Trade Accounts Payable
6335	Maintenance and Repairs	2131	Purchased and Contract Service Fees Payable
6338	Legal Notices and Other Publications		
6340	Printing and Office Supplies	2171	Due to General Fund
6344	Repair and Maintenance - Materials	2173	Due to Debt Service Fund
6349	Other Consumable Supplies and Materials	2175	Due to Taxpayers - Overpayment
		2176	Due to Assessor Collector - Tax Certificate
6350	Postage		
6351	Telephone	2701	Taxes Collected - Advanced Payments (Uncertified rolls)
6352	Utilities		
6353	Insurance and Surety Bond Premiums	2740	Deferred Revenues - Uncollected Debt Service Taxes
6354	Travel and Per Diem		
6357	Rents and Leases - Equipment		
6358	Rents and Leases - Space		Fund Balances
6359	Other Expenses		
6380	Transfer Fees - Connection Charges	3001	Allocated - Fund Net System Revenues
6399	Garbage Expense		
6600	Tap Connection Expense	3003	Interest Earnings Not Transferred
7306	Capital Outlay		
7362	Interest on Notes		Fund Transfers
7395	Miscellaneous Expense		
	TAX FUND	3911	Transferred to General Fund
		3913	Transferred to Debt Service fund
	Assets		Revenues
1110	Cash - Tax Collections	4320	Property Taxes
1140	Time Deposits - Tax Collections (includes certificates of deposit, saving certificates and saving accounts; details provided by schedule)	4321	Refund due Appraisal District Adjustment
		4322	Bank Franchise Tax
1141	Certificates of Deposit - Tax Collections	4331	Penalties and Interest on Tax Accounts
		4332	15% Penalty
1150	Tax Accounts Receivable	5380	Miscellaneous Income
1151	Tax Liens Receivable	5391	Interest on Temporary Investments

Sample Chart of Accounts – Continued

TAX FUND – Continued		Fund Balance	
	Expenses	3000	Reserved Fund Balance (for retirement of bond interest during construction)
6320	Legal Fees	3003	Interest Earnings Not Transferred
6330	Appraisal District	3009	Reserved for Bond Interest During Construction Period, _____ Issue
6331	Tax Assessor-Collector	3010	Reserved for Bond Interest During Construction Period, _____ Issue
6338	Legal Notice and Other Publications	3011	Reserved for Bond Interest During Construction Period, _____ Issue
6340	Printing and Office Supplies	3012	Reserved for Bond Interest During Construction Period, _____ Issue
6350	Postage	3013	Reserved for Bond Interest During Construction Period, _____ Issue
6353	Insurance and Surety Bond Premiums	3014	Reserved for Bond Interest During Construction Period, _____ Issue
7391	Foreclosure Costs	3030	Special Reserve
	DEBT SERVICE FUND		
	Assets		Fund Transfers
1110	Cash - Debt Service	3911	Transferred to General Fund
1121	Cash with Fiscal Agent (Paying Agent)	3914	Transferred to Capital Project Fund
1140	Time Deposits for Debt Service (includes certificates of deposits, savings certificates and saving accounts - details provided by schedule)	3951	Transferred from General Fund
1141	Certificates of Deposit for Debt Service	3952	Transferred from Tax Fund
1158	Accrued Investment Interest Receivable	3954	Transferred from Capital Projects Fund
1171	Due from General Fund		Revenues
1172	Due from Tax Fund	5391	Interest on Temporary Investments
1175	Due from Other Governmental Agencies		Expenses
1501	To be Provided for Bonded Debt	7360	Bond Interest Expense
	Liabilities	7362	Interest on Notes
2119	Accrued Interest Payable	7363	Fiscal Agent Fees (Paying Agent Fees)
2121	Tax Anticipation Notes Payable	7364	Bond Issue Expense
2131	Purchased and Contract Service Fees Payable	7369	Other Debt Service Expense
2135	Accrues Interest on Bonds at Date of Sale	7395	Bond Principal
2171	Due to General Fund		
2750	Unpresented Coupons		

APPENDIX H

Accounting Procedures and Requirements

General Fund-General Explanation

Purpose of Fund – The general fund is to be used for all operations of the district's water and wastewater system, including the related revenues from service installations, and should report all operating expenses of the district whether or not specifically related to the water and wastewater revenues. All the general and administrative expenses of the district should be reported in this fund whether or not paid from cash of the general fund. Additionally, any other activities of the district which do not belong in the other funds discussed herein should be accounting for in the general fund.

Classification of Expenses – A standard chart of accounts has been provided which classifies expenses between water, wastewater and other operating expenses (See **Appendix G**). These classifications are necessary in order to determine separately the cost of water and wastewater services for rate making and for obtaining governmental grants. It may be necessary to pro-rate some expenses between water, wastewater and other expense classifications. Also, the bookkeeper may need to require certain vendors and contractors to bill water and wastewater expenses separately.

General Fund-Water and Wastewater Billings General Fund-Returned Checks

Explanation – A water district generally bills monthly for the water and wastewater service it renders. The billing may be based on usage or on a flat rate.

Accounting Theory – Water and wastewater billings should be recorded monthly. The billing should include service through the end of the month or a date prior to the end of the month being recorded. If a service date after the end of the month is used, revenues are overstated and expenses are not properly matched with revenues. The district may elect to pro-rate revenue and expense for part of a month, but this is not generally necessary.

The district's billing agent may have a small amount of returned checks on hand at the end of the calendar month. Usually these checks will be part of the cash balance at month end. Older checks may have been charged back to accounts receivable. Returned check transactions should be included in the operating report from the billing agent and recorded in the general ledger. The balance outstanding at the end of the month should be reconciled to the list of returned checks furnished by the billing agent.

Records or Information Required – Operating report from the district's billing agent.

Accounting Procedures and Requirements

<u>Accounting Entries:</u>		<u>Dr.</u>		<u>Cr.</u>
<u>Billing Recorded</u>				
1110	Cash	XX		
1145	Service Accounts Receivable	XX	or	XX
1149	Returned Checks	XX	or	XX
4100	Customer Service Fees–Water			XX
4200	Customer Service Fees–Sewer			XX
4330	Penalties and Interest on Service Accounts			XX

The difference between beginning and ending Service Accounts Receivable should be recorded for the Service Accounts Receivable account. If the balance has increased, the entry should be a debit. If it has decreased, the entry should be a credit. Likewise, the net activity of Returned Checks should be recorded in this entry. If the total amount of returned checks receivable increased during the month, the entry should be a debit. If it has decreased, the entry should be a credit. Revenue accounts should be credited for the amounts billed for the month.

General Fund-Standby Charges

Explanation – Standby charges may be assessed by a water district on lot owners who have water and wastewater service available, but have not utilized service. It is a means of raising revenues for facilities which have been provided but are not being used. The earliest beginning date for such a charge would be during the earlier stages of the development of a district as established by the board of directors.

Accounting Theory – Standby charges generally should be recorded on the accrual basis in the general or debt service fund, depending on which fund the standby charge is dedicated. Although the district generally will collect these charges, the collection period may be relatively long and uncertain. In some cases, it may be necessary to report the revenues from standby charges on a cash basis.

Records or Information Required – Operating report from the district's billing agent.

<u>Initial Billing, Billed Separately Reported on an Accrual Basis</u>				
1157	Standby Charges Receivable	XX		
4500	Standby Charges			XX
<u>Billed Separately Reported on an Accrual Basis</u>				
1110	Cash	XX		
1157	Standby Charges Receivable	XX	or	XX
4500	Standby Charges			XX

The difference between Standby Charges Receivable at the beginning and end of the month should be debited if the end of month amount is greater, or credited if the beginning of the month amount is greater. Standby Charges should be credited for the amount billed.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>		<u>Cr.</u>
Billed as Part of Water and Sewer Billing Reported on an Accrual Basis			
1110 Cash	XX		
1145 Service Accounts Receivable	XX	or	XX
4500 Standby Charges			XX

Service Accounts Receivable should be treated as Standby Charges Receivable in the above entry. However, only receivable amounts pertaining to standby charges should be considered.

Initial Billing, Billed Separately Revenue Reported on a Cash Basis			
1157 Standby Charges Receivable	XX		
2750 Deferred Revenues-Uncollected Standby Charges			XX

Billed Separately Revenue Reported on a Cash Basis			
1110 Cash	XX		
1157 Standby Charges Receivable	XX	or	XX
2750 Deferred Revenues-Uncollected Standby Charges	XX	or	XX
4500 Standby Charges			XX

Standby Charges Receivable should be treated as above. If Standby Charges Receivable is debited, the Deferred Revenue account should be credited for the same amount. Likewise, if the Standby Charges Receivable account is credited, the Deferred Revenue account should be debited for the same amount. Cash should be debited and Standby Charges credited for the amounts actually received during the month.

General Fund – Allowance for Doubtful Accounts

Accounting Theory - In order to avoid overstating revenues at the date such amounts are recorded, an allowance for doubtful accounts should be provided for those amounts that may ultimately be uncollectible. If the amount that is considered to be doubtful is substantial, after considering the following factors, the allowance should be recorded. The following items enter into the decision to record an allowance for doubtful accounts:

1. Customer deposits – Security deposits may substantially offset any loss as a result of uncollectible accounts.
2. The collection policy of the district – Service may be discontinued after two months or after six months of unpaid charges, for example.
3. Collection experience of the district – This may be influenced by the economic status of the district and by the district's collection policy.
4. Delinquency Status – The age and amount of accounts outstanding for long periods such as 90 days or more.
5. Large accounts – Financial status of customers with substantial delinquent balances.

Accounting Procedures and Requirements – Continued

In many cases the conclusion will be reached that no allowance is necessary. It is certainly practical to omit the recording of an allowance if the effect on the balance sheet and revenues is not significant.

Records or Information Required – Operating report from the district's billing agent.

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Allowance Recorded</u>			
6155	Uncollectible Accounts	XX	
6255	Uncollectible Accounts	XX	
1146	Allowance for Uncollectible Service Accounts		XX

The Allowance account should be reviewed periodically to see that its level is appropriate given the current account balances and any other circumstances that may affect the collection of accounts.

Write-off of Uncollectible Accounts

1146	Allowance for Uncollectible Service Accounts	XX	
1145	Service Accounts Receivable		XX

The amount of this entry should correspond to the total of the specific Service Accounts Receivable balances to be written-off.

General Fund-Operating Reserve

Explanation – Some bond orders provide that a district establish an operating reserve to cover two months (or some other period of time) of operating expenses. Such bond orders may provide that the excess over the reserve be transferred to a special reserve fund (part of the debt service fund) until a specified amount has been accumulated in the special reserve fund.

Accounting Theory – In order for the water district to comply with the bond order requirement for an operating reserve, it is necessary for the district to estimate the required amount (two months operating expenses, for example) and record this amount in an operating reserve until cash in excess of liabilities exceeds this amount. When cash has been accumulated in excess of this reserve amount, the excess cash may be required to be transferred to the debt service fund. This should all be done through actions of the board of directors.

Records or Information Required:

1. Bond order
2. Board of directors determination of operating reserve requirement

Initial Establishment of Operating Reserve

3000	Unreserved Fund Balance	XX	
3005	Reserved for Operating Expenses		XX

The amount of this entry should be the amount which the board of directors has determined.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>		<u>Cr.</u>
<u>Adjustment of Operating Reserve</u>				
3000	Unreserved Fund Balance	XX	or	XX
3005	Reserved for Operating Expenses	XX	or	XX

A credit to the Reserve account #3005 should be made to increase the reserve and a debit made to decrease it. An equal offset should be made to the Unreserved Fund Balance account.

<u>Transferred to Debt Service Fund</u>				
3913	Transferred to Debt Service Fund	XX		
1110	Cash			XX

The entry should be made for any amount actually transferred which is in excess of the required reserve amount. Related Entry: Special Reserve-Debt Service Fund

General Fund-Taps Installations & General Fund-Sewer Inspection Fees

Explanation –

Taps Described

A tap is the line that runs from the district's main water and wastewater lines to a point in the yard of a house or building that will be constructed. The line may be designed to serve one (a single tap) or two (a double tap) customers. A normal tap (short tap) would be near the front of the lot, but in some instances, the tap may be towards the rear of the lot (long tap). A single tap is more expensive per tap, and most districts utilize the double tap.

Meter and Box

A meter and box must be installed prior to rendering water service. This generally is not done until the tap connection fee is paid and service is requested. When double taps are installed and only one customer requires service, only one meter is installed.

Installation of Taps

Generally, taps are installed as requested by builders, but some districts install taps for an entire street at one time. Occasionally, taps are installed during the construction phase with bond monies.

Taps Installed by Others

Occasionally, developers or builders may install taps which are reimbursable by the district or are donated to the district. The district may establish a tap fee rate order which excludes the tap or meter and requires the customer to pay the operator directly for such items.

Rate Order

Tap fees are established by a rate order which is passed by the board of directors. All charges should be made to customers based on this rate order.

Accounting Procedures and Requirements – Continued

Residential Tap

Tap fees for residential customers include the tap installation and the meter and box. This fee may include the wastewater inspection, although many districts collect a separate fee for this.

Commercial Tap

Commercial customers are generally charged a percentage of cost for tap installations (the type of installations vary substantially), plus a variable amount for the meter based on its size or cost. Commercial customers may also be charged an additional amount based on the square footage of land owned by the customer.

Accounting Theory –

General

In order to match revenue and expense, tap fee revenue and the related expense should be reported within the same accounting period. Although, theoretically, this matching of revenue and expense should be made on a monthly basis, this may not be practical. Thus, journal entries may be made only annually to defer revenue or expense.

Tap Fees and Expense

Tap fees should be reported in revenue as collected. A receivable for tap fees should be recorded if the district installed taps prior to collection. Tap expense should be accrued for installations made through the end of district's fiscal year.

Sewer Inspection Fees and Expense

Sewer inspection fees should be recorded on the cash basis. Wastewater inspection expense should be accrued as billed. Matching of these fees and expense may not necessary unless this practice substantially affects **net** revenues.

Taps Installed with Bond Money

The cost of taps installed with bond money in the construction fund should be transferred to the general fund and recorded as an asset of the general fund as Prepaid Tap Expense. This asset should then be charged to expense as the related tap fees are reported.

Taps Installed by Others

Reimbursable tap installations by the developers should be recorded as a liability of the general fund. If this amount is recorded as prepaid tap expense, it should be charged to expense as the applicable tap fees are recorded.

Theoretically, tap installations donated to the district may be reported in the general fixed asset fund as donated assets. Also, taps installed by customers or tap charges paid directly to operators by customers may be recorded in the general fixed asset fund. These transactions need to be recorded according to the accounting policies adopted by the district's board of directors under the advisement of the district's bookkeeper or auditor.

Accounting Procedures and Requirements – Continued

Prepaid or Deferred Taps

If the number of tap fees collected exceeds the number of installation costs accrued (expense), the excess number of fees collected should be deferred based on the amounts collected from customers. If the reverse situation occurs, the excess expense incurred should be deferred in the amount of cost of the tap installations to the district.

Unless the amount of prepaid or deferred taps is substantial, such amounts can be reversed in the month after year end and recorded again only at the designated interval. If they are substantial or if the district elects to be more precise, the prepaid amounts should be written-off to expense at the time the corresponding tap fees are reported. Likewise, deferred tap fees may be recognized as revenue at the time corresponding tap expenses are incurred.

Replacement of Taps and Meters

Replacements of meters or a reinstallment of a tap should be charged to repairs and maintenance. Any reimbursement received by the district should be reported as a credit to this expense account.

Records or Information Required–

1. Schedule of tap fees and expense designed to reconcile the number of installations received (tap fees) and installations accrued (tap expense).

	<u>Number of Installations</u>	
	<u>Fees</u>	<u>Expense</u>
Beginning of Year		
Deferred Fees	X	
Prepaid Expense		X
During the Year		
Fees Received	X	
Expense Accrued		X
Replacements		X
End of Year		
*Deferred Fees	(X)	
*Prepaid Expense		(X)
Number of Installations Reported in		
Revenues and Expenses	<u>X</u>	<u>X</u>

X indicates entry

(X) indicates end of period entry

The difference between the total number of tap fees and total number of tap expenses should be the number of replacements made during the period. After reconciling tap installations based on the number of connections, the proper amount of prepaid or deferred taps can be determined. Number of taps should be furnished by the district's operator.

2. Operating Report from the district's billing agent.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
TAP FEE REVENUE			
<u>Receipt of Tap Fees</u>			
1110	Cash	XX	
4600	Tap Connection Fees		XX
<u>Adjustment for Deferred Tap Fees</u>			
4600	Tap Connection Fees	XX	
2701	Tap Connection Fees-Advance Payments		XX
<u>Reversal of Deferred Tap Fees in following period</u>			
2701	Tap Connection Fees-Advance Payments	XX	
4600	Tap Connection Fees		XX
TAP EXPENSE			
<u>Payment of Tap Expense</u>			
6600	Tap Connection Expense	XX	
1110	Cash		XX
<u>Adjustment for Prepaid Tap Expense</u>			
1160	Prepaid Tap Expense	XX	
6600	Tap Connection Expense		XX
<u>Reversal of Prepaid Tap Expense in the following period</u>			
6600	Tap Connection Expense	XX	
1160	Prepaid Tap Expense		XX
OTHER TAP INSTALLATIONS			
<u>Taps Installed with Bond Money</u>			
6600	Tap Connection Expense	XX	
3954	Transferred from Capital Projects Fund		XX
Related Entry: Tap Installations-Capital Projects Fund			
<u>Reimbursable Tap Installation by Another Party</u>			
1160	Prepaid Tap Expense	XX	
OR			
6600	Tap Connection Expense	XX	
2110	Trade Accounts Payable		XX

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
SEWER INSPECTION FEES AND EXPENSE			
<u>Receipt of Sewer Inspection Fees</u>			
1110	Cash	XX	
4202	Service Inspection Fees		XX
<u>Payment of Sewer Inspection Charge</u>			
6275	Sewer Inspection Expense	XX	
1110	Cash		XX

General Fund-Maintenance Tax

Explanation - A maintenance tax may be assessed by the district to supplement the revenues of the general fund. It is levied as a part of the ad valorem tax based on values and may be collected in the general or tax funds. Below, entries necessary when maintenance taxes are collected by the tax fund are presented first. Entries necessary when maintenance taxes are collected directly by the general fund are then presented.

Accounting Theory - The maintenance tax should be accrued in the general fund as collected from the taxpayer by the tax fund unless ad valorem taxes are reported as levied.

MAINTENANCE TAXES COLLECTED BY THE TAX FUND

<u>Collection of the Maintenance Tax</u>			
1172	Due from Tax Fund	XX	
4320	Property Taxes		XX
4331	Penalties and Interest on Tax Accounts		XX

Entry should be in the amount of maintenance taxes actually collected by the Tax Fund. Related Entry: Tax Fund-General Explanation

<u>Transfer from the Tax Fund</u>			
1110	Cash	XX	
1172	Due from Tax Fund		XX

Entry should be for the amount actually transferred to the general fund. Related Entry: Tax Fund-General Explanation.

MAINTENANCE TAXES COLLECTED BY THE GENERAL FUND

<u>Levy of the Maintenance Tax</u>			
1150	Taxes Receivable	XX	
2740	Deferred Revenue-Uncollected Taxes		XX

Entry should be for the total amount of the maintenance tax levy.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
<u>Collection of the Maintenance Tax</u>		
1110 Cash	XX	
2740 Deferred Revenue-Uncollected Taxes	XX	
1150 Taxes Receivable		XX
4320 Property Taxes		XX

Entry should be for only those amounts actually received.

General Fund-Prepaid Insurance

Explanation – Insurance premiums are typically paid by water districts for a one year period.

Accounting Theory – In order to report insurance expense in accordance with the matching principle and to avoid the fluctuations in net revenues caused by the timing of payments, it is recommended that a water district amortize insurance premiums over the life of the policy. Due to the small amount involved, it will probably not be necessary to amortize fidelity bond premiums and small insurance endorsements.

<u>Payment of Insurance Premium</u>		
1161 Prepaid Insurance	XX	
110 Cash		XX

Entry should be for the entire amount paid.

<u>Monthly Amortization of Prepaid Insurance</u>		
6153 Insurance	XX	
6253 Insurance	XX	
6353 Insurance and Surety Bond Premiums	XX	
1161 Prepaid Insurance		XX

Entry should reflect one month of premium cost of one-twelfth of the yearly premium.

Tax Fund-Debt Service Taxes

Purpose of Fund – The tax fund has been established to account for the tax assessing and collecting functions of a water district. Legally, this fund is a part of the debt service fund and, generally, is not specified as a separate fund in the district's bond orders.

Use of Funds – Moneys in the tax fund can be used only to pay the expenses of collecting taxes and the balance of the fund must be transferred to the debt service fund, except for maintenance tax collections.

Accounting Theory – In order to report ad valorem tax revenues, these taxes should be available to pay the expenditures of the district.

Records or Information Required – Tax assessor/collector report.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
<u>Debt Service Tax Levied</u>		
1150 Tax Accounts Receivable	XX	
2740 Deferred Revenue-Uncollected Taxes		XX

Entry should be made for the total amount debt service taxes levied.

<u>Assessment of Penalties and Interest</u>		
1152 Tax Account Interest Receivable	XX	
1153 Tax Account Penalties Receivable	XX	
2740 Deferred Revenue-Uncollected Taxes		XX

<u>Collection of Taxes</u>		
1110 Cash-Tax Collections	XX	
2740 Deferred Revenue-Uncollected Taxes	XX	
6331 Tax Assessor-Collector Fees		XX
1150 Tax Accounts Receivable		XX
1152 Tax Account Interest Receivable		XX
1153 Tax Account Penalties Receivable		XX
4320 Property Taxes		XX
4331 Penalties and Interest on Tax Accounts		XX

Entry for Cash should include all amounts received by the district. The Deferred Revenue and the receivable accounts, respectively, should be debited and credited for the amounts actually paid by the taxpayers. This may be greater than the amounts received by the district due to tax collector fees.

<u>Adjustment of Roll</u>		
2740 Deferred Revenue-Uncollected Taxes	XX	or XX
1150 Tax Accounts Receivable	XX	or XX

An increase in the tax levy would cause a debt to Taxes Receivable and a decrease would cause a credit. An equal offset should be made to the Deferred Revenue account.

<u>Overpayment of Taxes</u>		
1110 Cash-Tax Collections	XX	
2175 Due to Taxpayers-Overpayment		XX

<u>Transfer of Cash to Debt Service Fund</u>		
3913 Transferred to Debt Service Fund	XX	
1110 Cash-Tax Collections		XX

Related Entry: Debt Service Fund-Transfer from Tax Fund

Accounting Procedures and Requirements – Continued

Tax Fund-Maintenance Tax

Explanation: A maintenance tax may be assessed by the district to supplement the revenues of the general fund. It is levied as a part of the ad valorem tax based on values and, generally, will be collected in the tax fund. Districts which collect their own maintenance tax in the general fund should see the general fund section for appropriate entries.

Accounting Theory – A maintenance tax is revenue to the general fund, and, thus, should not be reported as revenue by the tax fund. It should be recorded as payable to the general fund as collected. Although theoretically the costs of assessing and collecting maintenance taxes and penalties and interest on delinquent maintenance taxes should be reported separately from debt service taxes, such amounts are partially offsetting and usually insignificant and, thus, are generally not considered in reporting maintenance taxes owed to the general operating fund.

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Tax Roll Levied</u>			
1150	Tax Accounts Receivable	XX	
2740	Deferred Revenue-Uncollected Taxes		XX

Related Entry: Maintenance Tax-General Fund

<u>Assessment of Penalty and Interest</u>			
1152	Tax Account Interest Receivable	XX	
1153	Tax Account Penalties Receivable	XX	
2740	Deferred Revenue-Uncollected Taxes		XX

<u>Collection of Maintenance Tax</u>			
1110	Cash-Tax Collections	XX	
2740	Deferred Revenue-Uncollected Taxes	XX	
1150	Tax Accounts Receivable		XX
2171	Due to General Fund		XX

All amounts in this entry should be for the amount of maintenance taxes collected. Related Entries:
Maintenance Tax-General Fund

<u>Transfer to General Fund</u>			
2171	Due to General Fund	XX	
1110	Cash-Tax Collection		XX

Related Entry: General Fund-Maintenance Tax

Accounting Procedures and Requirements – Continued

Debt Service Fund-General Explanation

Purpose of Fund – The debt service fund was established by bond orders to accumulate resources for the retirement of bonded debt. Its resources are received from transfers from the tax fund or general fund and interest earnings. The bond orders and/or the TNRCC may require that interest earnings from other funds be transferred to this fund.

Accounting Theory – In accordance with the modified accrual basis of accounting, principal and interest expenditures should be reported when paid (cash basis). Interest revenues should be reported when earned and property taxes reported when received. In the examples below, it has been assumed that debt service taxes are being collected by the tax fund and then transferred to the debt service fund. Upon consolidation of the tax fund into the debt service fund for financial reporting purposes, the revenues recorded in the tax fund will be properly reflected in the debt service fund. If no tax fund is being used, the debt service tax entries shown in the tax fund section should be made in the debt service fund directly. Of course, no transfer of funds would then be necessary.

Records or Information Required – Paid bonds and interest coupons, or a cremation certificate in accordance with State statutes.

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Transfer from the Tax Fund</u>			
1110	Cash-Debt Service	XX	
3952	Transferred from Tax Fund		XX

Related Entry: Transfer to Debt Service Fund-Tax Fund

<u>Payment of Debt Due Upon Maturity</u>			
7360	Bond Interest Expense	XX	
7863	Fiscal Agent Fees	XX	
7395	Bond Principal	XX	
1110	Cash - Debt Service		XX

Debt Service Fund-Timing of Bond Payments

Explanation – If the water district's bonded debt is due on the date following year end, it frequently will be necessary for the district to pay its principal and interest requirements a few days in advance of the due date. Thus, the payment will occur within one fiscal year, whereas the due date of such payments is within the following year.

Accounting Theory – Once a water district transfers money to the paying agent, it should reduce the cash balance and recognize the payment as an expenditure of the debt service fund. The district no longer has control over these cash balances, and, legally, these funds are no longer assets of the district. Accordingly, principal and interest paid in one year which is due in the following year should be reported as an expenditure in the year paid. Debt service payments are being reported on a cash basis, and it not proper to report funds as assets on the district's balance sheet after transfer of the funds to the fiscal agent has taken place.

Accounting Procedures and Requirements – Continued

Debt Service Fund-Accrued Interest Received on Bonds at Date of Sale

Explanation – The interest from the date of the bonds up to the date of the sale is collected from the bond purchaser. This amount is remitted to the water district since the district will pay the bondholder interest accrued from the date of the bonds.

Accounting Theory – Interest accrued prior to the sale of the bonds is not revenue to the district since it had no cash invested for this period of time. Also, the district should not have interest expense for a period prior to the date of the sale of the bonds. Thus, accrued interest received at the date of the sale of the bonds should be recorded as a liability and offset against interest expense resulting in a net interest expense for the district from the date of the sale of the bonds through the interest coupon maturity date.

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Sale of Bonds</u>			
1110	Cash-Debt Service	XX	
2135	Accrued Interest on Bonds at Date of Sale		XX

Amount of this entry should be the amount if interest accrued from the data of the bonds through the sale date.

<u>Payment of First Interest Coupon</u>			
2135	Accrued Interest on Bonds at Date of Sale	XX	
7360	Bond Interest Expense	XX	
1110	Cash-Debt Service		XX

Bond interest expense recognized is for only the interest accrued from the sale date through the coupon maturity date.

Debt Service Fund-Bond Interest Reserve

Explanation – Many bond orders provide that funds sufficient to pay the district's bond interest during a specified period (usually two years) be set aside from the remainder of the bond issue proceeds and earmarked for the purpose of paying interest during the specified period.

Accounting Theory – The amount specified by the bond orders to pay the bond interest during the construction period should be deposited in the debt service fund and should be separately recorded as a bond interest reserve. If the bond orders provide for bond interest to be paid from this reserve from the date of the bonds, then the full amount of the first interest payment should be charged against this reserve. If the bond orders provide for the bond interest to be paid from the date of the sale of the bonds, then the amount charged to the bond interest reserve should be reduced by the accrued interest received on bonds at the date of the sale. Even though cash may not be physically segregated, it must be available for use exclusively as provided by the bond orders.

Records or Information Required – Bond order and related amortization schedule (relate amount deposited in debt service fund to interest due during the specified period).

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Sale of Bonds</u>			
1110	Cash-Debt Service	XX	
3009	Reserved for Bond Interest During Construction Period, ____ Issue		XX
<u>Payment of Interest from Reserve</u>			
7360	Bond Interest Expense	XX	
3009	Reserved for Bond Interest During Construction Period, ____ Issue	XX	
1110	Cash-Debt Service		XX
3000	Reserved Fund Balance		XX

All amounts in this entry should be for the amount of the interest payment.

Debt Service Fund-Special Reserve

Explanation – Bond orders frequently require that a water district accumulate, over a period of time, cash in a special reserve to be used only if the district is unable to otherwise meet debt service requirements. Cash for this reserve is generally deposited in the debt service fund without physical segregation of cash. The special reserve usually has one or more of the following characteristics:

1. The amount ultimately required in the reserve is subject to a maximum limit, such as the following year's debt service requirement or the average annual debt service requirement.
2. A fixed percentage of the principal and interest requirement is to be added to the reserve monthly using revenues from the general operating fund if available, or tax revenues if the revenues are not adequate.
3. Amounts are to be accumulated in the reserve to the extent that cash in the general operating fund exceeds what is needed to pay two months operating expenses.

Accounting Theory – A general ledger account should be established to account for the amount in the debt service fund which has been accumulated to meet the requirements of the special reserve. Amounts transferred to the debt service fund which have been identified as being part of this reserve and other amounts in the debt service fund not necessary to meet current maturities should be transferred to this reserve until adequate resources are accumulated.

Records or Information Required - Board of directors resolution approving transfers to the special reserve.

Transfer from General Fund for Special Reserve			
1110	Cash-Debt Service	XX	
3000	Reserved Fund Balance	XX	
3030	Special Reserve		XX
3951	Transferred from General Fund		XX

All amounts in this entry should reflect the amount transferred from the general fund.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
<u>Transfer of Amounts in Debt Service Fund to Special Reserve</u>		
3000 Reserved Fund Balance	XX	
3930 Special Reserve		XX

Capital Projects Fund-General Explanation

Purpose of Fund – The purpose of the Capital Projects Fund is to account for the financial resources designated to construct or acquire capital facilities and improvements. Such resources are derived principally from proceeds of the sale of bonds.

Accounting Theory – Implementation of the modified accrual basis of accounting for the Capital Projects Fund does not present any changes in the transactions recorded or the timing of those transactions from those that would be recorded using the full accrual method.

Uses of Proceeds – The cash received from the sale of bonds must be spent in accordance with the requirements of the Texas Water Code (State statutes), the applicable bond order and the applicable engineering estimate approved by the Texas Natural Resource Conservation Commission.

Sale of Bonds

1110 Cash-Capital Projects Fund	XX	
3955 Proceeds from Sale of Bonds		XX

Related Entries: General Long-Term Debt-General Explanation
 Capital Projects Fund-Escrowed Cash
 Debt Service Fund-Accrued Interest Received on Bonds at Date of Sale
 Debt Service Fund-Bond Interest Reserve

Payment for Construction Costs

7300 Capital Outlay, _____ Bond Issue	XX	
1110 Cash-Capital Projects Fund		XX

Total amount of expenditure should be recorded as capital outlay regardless of whether the whole amount will be capitalized in the General Fixed Asset Account Group. In this entry, it is assumed here that the construction costs are not to be reimbursed by another party. See “Developer Contributions-Capital Projects Fund.”

Payment of District Organizational Costs

7300 Capital Outlay, _____ Bond Issue	XX	
1110 Cash-Capital Projects Fund		XX

As above, the total amount of organizational costs should be recorded as capital outlay regardless of the district’s policy of capitalizing organizational costs.

Related Entry: General Fixed Assets Account Group-General Explanation

Accounting Procedures and Requirements – Continued

Capital Projects Fund-Escrowed Cash

Explanation – In connection with the sale of bonds, water districts may be required by the Texas Natural Resource Conservation Commission to escrow (place in the custody of a third party) a portion of the proceeds from the sale of bonds. Also, cash may be escrowed in connection with a joint construction project between two water districts. The accounting records of a district should distinguish between funds which are available for expenditure and those held in escrow. Escrowed funds are typically released upon satisfactory completion of a project or the occurrence of some other specified event.

Accounting Entries:		Dr.	Cr.
<u>Placement of Funds in Escrow</u>			
1122	Cash in Escrow	XX	
1110	Cash-Capital Projects		XX

If funds are placed in escrow at the same time that bond proceeds are received, this entry can be performed in conjunction with the entry for the receipt of bond proceeds.

<u>Release of Escrow Funds</u>			
1110	Cash-Capital Projects	XX	
OR			
2130	Construction Contracts Payable	XX	
1122	Cash in Escrow		XX

The appropriate debit will be made depending on whether funds are paid out of the escrow fund or returned to the district's cash account for payment.

Capital Projects Fund-Contracts Payable

Explanation – In connection with the construction of facilities, the water district is billed monthly for 100% of construction work done, but is required to pay on a timely basis for usually only 90% of the work done with the remaining 10% being due after completion of the facilities. This 10% portion is referred to as retainage.

Accounting Theory – The full cost of construction should be recorded as the work progresses, whether or not the amount is due now or at a subsequent date. As a practical matter, if the contractor bills through a date subsequent to the end of the district fiscal year, it generally will not be necessary to pro-rate these amounts through year end unless the amounts are unusually large or the period of time is for a month or more.

CONSTRUCTION INVOICES ACCRUED PRIOR TO PAYMENT

<u>Construction Draw Accrued</u>			
7300	Capital Outlay, _____ Bond Issue	XX	
130	Construction Contracts Payable		XX
2140	Construction Contracts Payable, Retained Percentage		XX

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
<u>Construction Draw Paid</u>		
2130 Construction Contracts Payable	XX	
1110 Cash-Capital Projects Fund		XX

CONSTRUCTION INVOICE NOT ACCRUED PRIOR TO PAYMENT

<u>Construction Draw Paid</u>		
7300 Capital Outlay, _____ Bond Issue	XX	
1110 Cash-Capital Projects Fund		XX
2140 Construction Contracts Payable, Retained Percentage		XX

BOTH SCENARIOS

<u>Payment of Construction Retainage</u>		
2140 Construction Contracts Payable, Retained Percentage	XX	
1110 Cash-Capital Projects Fund		XX

Capital Projects Payable-Bond Anticipation Notes Payable

Explanation—Bond anticipation notes payable may be issued for any purpose for which bonds of the district may have previously been voted or may be issued for the purpose of refunding previously issued bond anticipation notes. The district may agree with the purchaser of the note that the district will use the proceeds of any sale of bonds to retire these notes. The rates and terms are prescribed by State statutes.

Accounting Theory – Bond anticipation notes should only be recorded as a liability of the Capital Projects Fund if the district has **not** taken all legal steps necessary to refinance the bond anticipation notes **or** if the district does **not** have the ability or intent to refinance the note on a long-term basis. If legal steps have been taken and the ability and intent of the district is present, the bond anticipation notes should be recorded as liabilities of the General Long-Term Debt Account Group.

Records or Information Required – Copy of bond anticipation note and receipt of funds.

<u>Proceeds of Notes</u>		
1110 Cash-Capital Projects Fund	XX	
2150 Bond Anticipation Notes Payable		XX

<u>Accrual of Interest</u>		
7362 Interest Expense on Notes	XX	
2119 Accrued Interest Payable		XX

Interest should be recorded on the accrual basis of accounting.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
	<u>Payoff of Note</u>	
2119 Accrued Interest Payable	XX	
2150 Bond Anticipation Notes Payable	XX	
1110 Cash-Capital Projects Fund		XX

Capital Projects Fund-Developer Contributions

Explanation – Developers are being required by the Texas Natural Resource Conservation Commission to contribute to the district an amount generally equal to 30% of the cost of drainage, water lines, wastewater lines, and related engineering costs as a condition for the Commission’s approval of bonds. In some cases, the developer may advance funds on behalf of the district and accept reimbursement net of the portion of the cost to be paid by the developer. In other cases the district will pay all costs and bill the developer for his part. The developer and the district may also pay their respective parts directly to the contractor and/or engineer.

Accounting Theory – Only expenditures made by the district should be recorded as capital outlay in the records of the district. Construction and other costs paid directly by another party are not expenditures of the district, although they may be recorded as fixed assets in the district’s General Fixed Asset Account Group. Reimbursements to the district by the developer should be recorded as developer contributions and should not be recorded as a credit to the asset cost.

Receivable from Developer – Developer contributions should be accrued as the related construction costs are incurred by the district, including that part related to retainage. Exclusion of developer receivables understates the district’s remaining resources. Since the district generally does not bill the developer until payment is due by the district, it is recommended that amounts due currently and deferred amounts due be charged to separate accounts.

Records or Information Required–

1. Invoices approved by the district’s engineer specifying the part to be paid by the developer and the district.
2. Engineering estimate specifying costs to be shared by the developer.

CONSTRUCTION COSTS PAID DIRECTLY BY THE DEVELOPER TO THE CONTRACTOR

	<u>Reimbursement Paid to Developer by District</u>	
7300 Capital Outlay, _____ Bond Issue	XX	
1110 Cash-Capital Projects Fund		XX

Only expenditures of the district should be classified as capital outlay. No capital projects fund entry is necessary when non-reimbursable construction is performed by the developer. See General Fixed Asset Account Group section for appropriate entries.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
CONSTRUCTION COSTS PAID DIRECTLY BY DISTRICT			
<u>Accrual of Developer Contribution</u>			
1177	Due from Developer - Currently Due	XX	
1178	Due from Developer - Deferred (Retainage)	XX	
3956	Developer Contributions		XX

This entry should be performed in conjunction with the recognition of capital outlay costs. See “Capital Projects Fund-General Explanation” and “Contract Payable-Capital Projects Fund.”

<u>Receipt of Cash from Developer</u>			
1110	Cash - Capital Projects Fund	XX	
1177	Due from Developer - Currently Due		XX

Capital Projects Fund-Interest Earnings

Explanation – The disposition of interest received by the Capital Projects fund is governed by State statute and the district’s bond orders. Transfer of interest on TNRCC approved bonds to another fund will require application to and approval by the TNRCC.

<u>Interest Accrued</u>			
1158	Accrued Investment Interest Receivable	XX	
5391	Interest on Temporary Investments		XX

<u>Interest Received</u>			
1110	Cash-Capital Projects Fund	XX	
1158	Accrued Investment Interest Receivable		XX

<u>Transfer to Debt Service Fund Upon TNRCC Approval</u>			
3913	Transferred to Debt Service Fund	XX	
1110	Cash-Capital Projects Fund		XX

Capital Projects and General Funds-Sale of Fixed Assets

Accounting Theory – The proceeds from the sale of fixed assets should be deposited into the capital projects fund and used to complete construction projects, if necessary. If not necessary to complete construction projects, the proceeds may be deposited into the general fund and used for operating expenses.

CAPITAL PROJECTS FUND

<u>Proceeds from Sale of Fixed Assets</u>			
1110	Cash-Capital Projects Fund	XX	
3960	Sale of Fixed Assets		XX

Related Entry: Sale or Replacement of Fixed Assets-General Fixed Asset Account Group

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
GENERAL FUND			
<u>Proceeds from Sale of Fixed Assets</u>			
1110	Cash	XX	
3960	Sale of Fixed Assets		XX

Related Entry: Sale of Replacement of Fixed Assets-General Fixed Asset Account Group

Capital Projects Fund-Costs to be Reimbursed from Future Bond Sales

Accounting Theory – Costs to be reimbursed to attorneys, engineers, developers, contractors, etc. from future bond sales, should be recorded **unless** the contract or agreement between the parties specifies that reimbursement is due only upon the sale of bonds. Liabilities which are due only upon the occurrence of a particular event are termed “contingent liabilities.” Although these liabilities are not recorded, documentation must be kept on these items for audit purposes and for proper recording upon the occurrence of the contingent event.

All Funds-Closing Entries

To facilitate the performance of the audit, the district’s auditor will prefer that revenue, expense and fund balance transactions not be closed to the balance sheet accounts prior to the audit. Before posting any transactions in the following fiscal year, these accounts must be closed to the appropriate fund balance accounts. After closing and any adjusting entries have been posted, the balance sheet accounts should be reconciled to the audit report.

In a manual system, closing entries can be provided by the district’s auditor. The workpaper package provided when each audit is completed should include all appropriate journal entries to close and adjust applicable balances, so that the district’s records will agree with the audited financial statements.

If a computerized system is used, it may not be possible to make adjustments to the records of the fiscal year under audit at the time the audit is completed. In this instance, corrections to the records must be made to the following fiscal year’s records.

All Funds-Interfund Loans and Transfers

Accounting Theory – Cash moved between funds and expenses paid by one fund for another fund should be reported as interfund loans (reimbursable) if the following criteria are met:

1. There is intent to repay the amount, and such intent is documented by minutes, subsequent repayment, etc...

-and-

2. The debtor fund has, or is likely to have, adequate resources to repay the amount within a reasonable time period.

Accounting Procedures and Requirements – Continued

Cash moved to or expenses paid for another fund which do not meet these criteria should be reported and interfund transfers.

If the transaction qualifies as a loan, it should be shown as a receivable and payable on the balance sheet if outstanding at year end, and, thus, would not affect the fund balance of either fund.

If the transaction is to be reported as an interfund transfer, the fund balances of the applicable funds are affected and no amounts are reported in the balance sheet. If subsequent repayment is made, it is reported as a contra-transfer.

When one fund pays an expense which should be paid by another fund, in accordance with its stated purpose, the transaction should be reported as an interfund transfer or loan so that the expense can be reported in the proper fund.

If the debt service or tax fund loans money to another fund, then the bond order provision requiring that tax collections be used only for debt service (maintenance taxes excepted) and expenses of collection has been violated. Whether the loan is repaid by the other fund within the fiscal year is not relevant. If the debt service or tax fund receives money from another fund and then repays that loan, the bond order provision has not been violated. Check each bond order separately since it governs interfund transactions.

Records or Information Required:

1. Bond Order
2. Position of board in regard to repayment of loans

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Payment Made for Another Fund Repayment Not Anticipated</u>			
GENERAL FUND ENTRY:			
3913	Transferred to Debt Service Fund	XX	
1110	Cash		XX
DEBT SERVICE FUND ENTRY:			
7360	Bond Interest Expense	XX	
7395	Bond Principal	XX	
3951	Transferred from General Fund		XX

These entries would be made if the General Fund were to pay the bond payment for the Debt Service Fund with no repayment to be made by the Debt Service Fund.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
Transfer of Funds Repayment Not Anticipated		
CAPITAL PROJECTS FUND ENTRY:		
3913 Transferred to Debt Service Fund	XX	
1110 Cash-Capital Projects		XX
DEBT SERVICE FUND ENTRY:		
1110 Cash-Debt Service	XX	
3954 Transferred from Capital Projects Fund		XX

These entries would be made when Capital Projects Fund surplus funds are transferred to the Debt Service Fund after obtaining TNRCC approval.

Interfund Loan, Repayment Anticipated Loan Originated		
GENERAL FUND ENTRY:		
1173 Due from Debt Service Fund	XX	
1110 Cash		XX
DEBT SERVICE FUND ENTRY:		
1100 Cash-Debt Service	XX	
2171 Due to General Fund		XX

Interfund Loan, Repayment Anticipated Loan Repaid		
GENERAL FUND ENTRY:		
1110 Cash	XX	
1173 Due from Debt Service Fund		XX
DEBT SERVICE FUND ENTRY:		
2171 Due to General Fund	XX	
1100 Cash-Debt Service		XX

All Funds-Accounts Payable

Explanation - In this section, it will be assumed that the district does not normally use accounts payable, but records purchases on a cash basis and makes adjustments to accrue accounts at year end to bring the records into conformity with the modified accrual basis. Thus, accounts payable would represent the accrued liability for goods or services received during the year for which payment has not been made as of the end of an accounting period. This would include amounts not billed to the district on a timely basis.

Accounting Procedures and Requirements – Continued

Accounting Theory – In order to be on a modified accrual basis, the district must record all expenses incurred by the district through the fiscal year end. The districts bookkeeper should search the district's records through a period subsequent to year end to determine that all significant expense expenditures have been recorded and make specific inquiries in regard to work done or services rendered to the district through the end of the fiscal year (legal fees, operating fees) which have not been billed timely to the district.

The most practical way for districts to record accounts payable will be by utilizing the make and reverse principle. Under this principle, for example, accounts payable would be recorded by debiting the expenditure account and crediting accounts payable at the end of the district's fiscal year (current period). In the following fiscal year, the entry made is reversed (accounts payable is debited, expenditure account is credited). Upon payment, the same expenditure account should be debited for the amount of the disbursement. The debit to the expenditure account from cash disbursements will be offset by the credit made when reversing accounts payable, leaving only the original debit to expense made from the first entry in the proper fiscal year's recorded.

<u>Accounting Entries:</u>		<u>Dr</u>	<u>.Cr.</u>
<u>Accrual of Accounts Payable At the End of the Fiscal Year</u>			
6320	Legal Fees	XX	
2110	Trade Accounts Payable		XX

In this General Fund example, legal fees incurred by the district in the fiscal year had not been paid by the end of the fiscal year. It is not relevant whether the legal fees had been billed by the fiscal year end date. The date that the charges were incurred determines whether the changes relate to the current fiscal year or the subsequent.

<u>Reversal of the Accrual Entry At the Beginning of the Subsequent Year</u>			
2110	Trade Accounts Payable	XX	
6320	Legal Fees		XX
<u>Upon Payment of the Charges</u>			
6320	Legal Fees	XX	
1110	Cash		XX

The net effect of these entries is to record an expenditure in the earlier fiscal year when the charges were actually incurred. This method can be used for the other funds using the appropriate comparable accounts.

General Long-Term Debt Account Group-General Explanation

Purpose of Fund – The fund was established to report the principal amount of general obligation debt due in future years by a water district.

<u>Bonds Sold</u>			
1500	To be Provided for Bonded Debt	XX	
2510	Bonds Payable, Series _____		XX

Accounting Procedures and Requirements – Continued

Entry should reflect the total principal amount of bonds issued. Discounts and/or premiums should not be considered in this entry.

Related Entries: Capital Projects Fund–General Explanation
 Capital Projects Fund–Escrowed Cash
 Debt Service Fund–Accrued Interest Received on Bonds at Date of Sale
 Debt Service Fund–Bond interest Reserve

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
		<u>Bonds Paid</u>
2510 Bonds Payable, Series _____	XX	
2511 Bonds Payable, Series _____	XX	
1500 To Be Provided for Bonded Debt		XX

Amounts in this entry should reflect only principal amounts paid.

Related Entry: Debt Service Fund-General Explanation

General Fixed Asset Account Group-General Explanation

Purpose of Account Group – The General Fixed Asset Account Group is designed to account for the district’s facilities (whether located inside or outside of the district’s boundaries). This includes tangible costs, such as water, wastewater and drainage systems, and intangible costs, which are called district organizational costs.

Accounting Theory—All costs related to the organization of a district, sale of bonds or construction of district-owned facilities should be capitalized with the possible exception of infrastructure assets. Legal fees should be capitalized only if they meet these criteria. This construction period is usually one year from the date of the sale of bonds, but may be substantially shorter or longer. The costs of facilities should be capitalized as they are incurred. Even the costs of incomplete facilities (construction in progress) should be capitalized when incurred.

In order to facilitate the tracking of resources provided for the purchase of fixed assets (i.e., bond proceeds, system revenues), an appropriate designation should be made in the fund equity section of the General Fixed Asset Account Group.

Physical plant (tangible costs) include land, buildings, equipment, water, wastewater and drainage facilities, and related engineering costs. These accounts represent direct costs of construction facilities.

If the facilities are jointly owned by two or more districts, record only the part owned by the applicable district as an asset on its books. If plant capacity is merely being leased to another district, the full cost of the facilities should be recorded as an asset of the lessor district.

It may be required that a district capitalize the cost of acquiring capacity in another district for a specified term. The cost to be capitalized would exclude any amounts paid for operating expenses. The specific terms of the lease will determine whether capitalization is necessary.

Accounting Procedures and Requirements – Continued

District organizational costs (intangible costs) are the costs of organizing a district, selling its bonds, and financing construction of the district's assets. Organizational costs include bond interest, legal fees, election costs, interest paid to developer, etc.

Interest expense and earnings (related to the applicable bond sale proceeds) are capitalized until substantial completion of facilities in order to reflect the net financing cost of the district's facilities in the General Fixed Asset Account Group (GFAAG).

District organizational costs should be recorded as capital outlay in the capital projects fund at the same time they are recorded as assets of the district in the GFAAG.

Records or information Required–

1. Construction in progress list or ledger
2. General fixed asset list or ledger

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
<u>Organizational Costs Incurred by District</u>			
1401	Organizational Costs – Legal Fees	XX	
1413	Organizational Costs – Election Costs	XX	
1415	Organizational Costs – Other Costs	XX	
3010*	Investment in Fixed Assets – From Sale of Bonds		XX
3011*	Investment in Fixed Assets – Contributed by Developer		XX

* Account used for the credit portion of this entry should indicate the source of the funds used acquire the fixed asset in the debit portion of this entry, whichever account(s) is applicable. See suggested Chart of Accounts located in **Appendix G** of this manual for a complete list of the organizational cost and investment in fixed asset accounts.

<u>Bond Interest and Investment Interest Capitalization</u>			
1403	Organizational Costs – Bond Interest	XX	
1411	Organizational Costs – Interest on Temporary Investments		XX
3010	Investment in Fixed Assets – From Sale of Bonds		XX

Account 1403 should be debited for interest on bonds (and other related debt) up to the time that the facilities financed by the bonds are substantially complete. Interest revenues related to bond proceeds during the same period should be reflected in Account 1411 of this entry.

CONSTRUCTION IN PROGRESS ACCOUNT NOT USED

<u>Facility of System Completed Not Previously Construction in Progress</u>			
1312	Water System	XX	
1313	Sewer System	XX	
1314	Drainage System	XX	
3010	Investment in Fixed Assets – From Sale of Bonds		XX

All of the accounts listed above will vary according the type of facilities and the source of funds used to acquire the assets.

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>	<u>Dr.</u>	<u>Cr.</u>
CONSTRUCTION IN PROGRESS ACCOUNT USED		
<u>Construction Costs Incurred by District</u>		
1351 Construction in Progress, _____ Bond Issue	XX	
3010 Investment in Fixed Assets – From Sale of Bonds		XX

The credit portion of this entry will vary depending upon the source of funds use to finance the construction.

<u>Facility or System Completed Previously Construction in Progress</u>		
1312 Water System	XX	
1313 Sewer System	XX	
1314 Drainage System	XX	
1351 Construction in Progress, _____ Bond Issue		XX
3010 Investment in Fixed Assets - From Sale of Bonds		XX

The accounts debited in this entry will vary according the type of facilities constructed. All construction in progress amounts related to the facilities completed and reflected in the debit portion of this entry should be closed-out to zero with the credit to construction in progress. The account used for investment in fixed assets will vary depending upon the source of funds used to finance the facilities. The credit to investment in fixed assets should reflect only amounts which were not previously recorded in construction in progress.

<u>Sale of Fixed Assets</u>		
3010 Investment in Fixed Assets – From Sale of Bonds	XX	
1312 Water System		XX

Amounts in this entry should reflect the original cost of the asset sold as recorded in the district’s fixed asset ledger. The account used for investment in fixed assets should will depend upon the source of funds used to finance the original purchase of the asset being sold.

General Fixed Asset Account Group-Tap Installations

Accounting Theory – Tap installations (described in section titled “Tap Installations-General Fund”) are part of the water district’s distribution system and, thus, should be capitalized in the general fixed asset account group. Since the customer pays a fee related to this installation, which is reported as revenue in the general operating fund, such assets are shown as being provided by net system revenues.

The cost of tap installations is generally not allocated on the invoice between the water and sewer tap. This cost can be allocated based on an estimate by the operator.

<u>Tap Installations Capitalized Paid by General Fund</u>		
1312 Water System	XX	
1313 Sewage System	XX	
3001 Investment in Fixed Assets-From Net System Revenues		XX

Accounting Procedures and Requirements – Continued

<u>Accounting Entries:</u>		<u>Dr.</u>	<u>Cr.</u>
Tap Installations Capitalized			
<u>Paid Direct to Operator by Customer</u>			
1312	Water System	XX	
1313	Sewage System	XX	
3001	Investment in Fixed Assets-From Net System Revenues		XX
Tap Installations Capitalized			
<u>Paid with Bond Moneys</u>			
1312	Water System	XX	
1313	Sewage System	XX	
3010	Investment in Fixed Assets-From Sale of Bonds		XX
Related Entry: Tap Installations-Capital Projects Fund			
Tap Installations Capitalized			
<u>Donated by Developer</u>			
1312	Water System	XX	
1313	Sewage System	XX	
3011	Investment in Fixed Assets-Contributed by Developer		XX

APPENDIX I

District Records

Due to the segmented nature of the activities of a water district, generally no one individual maintains all the required records and information. The following lists of records and information are those necessary for an audit. As a guide, they have been divided according to the individuals responsible for originating or maintaining these records. Each district should establish responsibility for these records according to its own particular situation.

I. The Bookkeeper:

A. Primary Accounting Records:

1. General Ledger - Should be segregated as to the six funds and should be coded in accordance with the numerical chart of accounts.
2. Cash Receipts Journal - All resources of a district should be classified in this journal in accordance with the numerical chart of accounts.
3. Cash Disbursements Journal - All expenditures of a district should be classified in this journal in accordance with the numerical chart of accounts.
4. General Journal or Journal Vouchers - All journal entries should be adequately explained and approved by a designated person and referenced in the general ledger. Appropriate supporting documentation should be provided and filed in the same sequence as the entries are recorded. If journal vouchers are used, they should be numbered and filed numerically.
5. Cash Receipts Documentation - The district's bookkeeper should maintain all applicable documentation in regard to cash receipts.
6. Cash Disbursements Documentation - The district should maintain copies of checks or checkbook stubs in numerical order. Expenditure information, such as invoice numbers and a brief description or explanation of the transaction, should be entered on the check copy or checkbook stub. Invoices, or other documentation supporting all expenditures, should be maintained in either numerical or alphabetical order and coded using the numerical chart of accounts. Paid bonds and bond coupons, or cremation certificates relative to bonds and coupons, should be maintained by the district.
7. Accounts Receivable Subledger - A detailed subsidiary record should be maintained if multiple customers are included in one general ledger account, and such subsidiary records should be in agreement with the general ledger. These records need not repeat any of the subsidiary records maintained by others, such as the billing agent or tax assessor-collector.
8. Current Investment Journal - A schedule showing all transactions by fund should be provided. Copies of applicable certificates of deposit and savings account statements should also be maintained.

9. Accounts Payable Subledger - A subledger or list is needed if multiple vendors are included in one general ledger account, and such subledger or list should be in agreement with the general ledger.
10. Reconciled Monthly Bank Statements - All accounts should be reconciled monthly and reconciliations should be retained. (**Appendix M**).
11. Security Ledger - A ledger showing all securities pledged and released by financial institutions. Copies of safekeeping receipts and related releases should be maintained.
12. Fixed Asset Ledger - A detailed listing showing each fixed asset, description, identification number, date placed into service and cost.

B. Other Special Journals and Records:

1. Payroll Journal - Must include employee name, social security number, classification, exemptions and/or deductions, and net pay. This journal may be used if a district has several employees.
2. Purchase Journal - If a district has a large number of purchases monthly, this journal may be necessary as an internal control for all purchases. Purchase orders may be issued on all purchases over a certain amount. Purchase orders should be prenumbered and have specific approvals.
3. Investment Records - Any backup paperwork, such as safekeeping receipts for certificates of deposits.
4. Operator Reports - Used for posting to the general ledger.
5. Tax Collector Reports - Used for posting to the general ledger.
6. Bookkeeping Reports - Submitted to board monthly.
7. Audits - Copies kept to cross-reference current work with prior years.
8. Bond Sale Records - Records pertaining to the district's bond sales, official statements, amortization schedules and documentation for all bond sale disbursements.
9. Legal Contracts - Involving other governmental units. Escrow agreements and releases should be reviewed for proper accounting.
10. Minutes - Should be reviewed to make certain that any special directions are followed.
11. Inspection of Facilities Report - Performed by the district's engineer.
12. Bond Amortization Schedules - Supplied by district's fiscal agent for each bond issue.

II. Operator/Billing Agent:

- A. Tap Journal - Records should be maintained in such a manner that tap fees collected can be identified with taps installed. The journal should include:
1. Date cash received for the tap.
 2. Name of person or company ordering the tap.
 3. Service address and legal description of location of the tap.
 4. Date tap installed.
 5. Serial number of meter installed.
 6. Account number assigned to the service address.
 7. Date the cost of tap installation was billed to the district.
 8. The receipt number and amount received for the tap installation.
 9. Date sewer inspection was performed.
- B. Monthly Billing Records - Should include the following:
1. Monthly current billing and cash receipts.
 - a. Identified as to water, sewer, penalty, surcharge, application fee, garbage, EMS, customer deposits, etc.
 - b. Standby Billings - Identified by current billing and any penalty and interest.
 - c. Builder Damages - Separate record of damages reflecting date of damage, person responsible, cost of repair and date of billing should be maintained if the district is in an active building program.
 2. Monthly Billing Adjustment Register.
 - a. Authorized approval (ie, manager of district)
 - b. Detail of returned checks
 3. Accounts Receivable Ledger identified by customer.
 4. Monthly billed water usage in gallons.
 5. Cash receipts listing of customer payments.

6. Number of customers in district.
 7. Operator Reports - Submitted to the board by district bookkeeper.
- C. Rate Order - Date adopted by board of directors and effective date should be noted.
 - D. Map of District - All lots marked with an account number in an order that will facilitate meter reading.
 - E. Meter Books - With meter reading sheets for regular customers should be maintained.
 - F. Security Deposits - List by customer, legal description or address, date of receipt and amount of all deposits on file and total should be maintained. Bookkeeper should ensure that the total is in agreement with the general ledger.

III. Tax Collector:

- A. Tax Rolls - Original roll for each year the district has levied taxes should be maintained.
- B. Delinquent Rolls - Roll showing all outstanding taxes by years, as of the fiscal year end.
- C. Tax Receipts - Paid receipts grouped by date of deposit.
- D. Deposit Slips - Copy of deposit slip attached to applicable group of receipts.
- E. Bank Statements - Should be maintained for all tax accounts maintained during the year and be filed in date order in a separate bank statement folder. Bank statements reconciled on a monthly basis should include outstanding checks and deposits in transit and should be dated and signed.
- F. Checkbook - Should be reconciled monthly to bank statement.
- G. Source Documents - Payments to vendors should be made from original invoices. Original invoices should be verified for accuracy and signed. All paid invoices should be canceled by showing date paid and check number and should be filed in an orderly fashion.
- H. Monthly Tax Reports - Should be furnished to the bookkeeper with information to properly record the district's assessments, collections, and disbursements. The information on the report should indicate the following:
 1. All cash transactions reported and reconciled with beginning and ending balances.
 2. Cash receipts and disbursements coded using a consistent chart of accounts.
 3. Taxes receivable reported by years and all changes shown.
 4. Maintenance taxes receivable and collections should be accounted for separately from debt service taxes.
 5. Collections and refunds of overpayments should agree with the amounts included in the cash receipts and disbursements section of the report.

IV. Attorney:

- A. Minutes - approved by the board of directors.
- B. Bond Orders
- C. Rate Orders
- D. Board Member Information - Terms and addresses.
- E. Fidelity Bond Coverage - Directors, bookkeepers and tax assessors.
- F. Construction Contracts
- G. Order Establishing New Depositories
- H. Grant Applications (unless provided by engineer to bookkeeper)
- I. Developer Contributions - TNRCC order and agreement with developer.
- J. Engineer's Inspection of Facilities
- K. Notes - Paid notes and copies of unpaid notes.
- L. Escrow Agreements - TNRCC agreement, other contractual agreements, escrow agreement with bank, release of escrowed funds.
- M. Insurance Policies - Physical damage and general liability.
- N. Certificates of Insurance
- O. Deeds for Land Acquired
- P. Any Other Contracts (not cited above)

V. Engineer:

All records or information needed for the auditor should be furnished to the district's attorney or bookkeeper.

VI. Investment Officer:

Investment Reports—quarterly written reports are required by the Public Funds Investment Act to be provided by the investment officer to the district (**Appendix C**).

APPENDIX J

Suggested Records Retention Schedule

<u>Type of Record</u>	<u>Years Recommended</u>
ACCOUNTING	
Accounts Payable (Vouchers) Invoices & Credits (assuming that there are no pending audits)	5
Assets Purchased File (after disposal)	5
Audit Files (contains audit correspondence and reports)	20
Audit Work Papers	20
Bank Statements and Reconciliations	5
Bond, Bondholder's Records, Transcripts, and Bond Resolutions	Permanent
Bond and Coupon Certificates of Destruction	Permanent
Bonds and Notes - Canceled and Paid Interest Coupons	5
Bonds - Record of Interest Coupons	5
Bookkeeper's Reports	5
Budgets and Comparison Reports	5
Budget File	5
Canceled Checks	5
Cash Disbursements File	5
Cash Disbursements Journal	Permanent
Cash Disbursements Source Document	5
Cash Receipts File	5
Cash Receipts Journal	Permanent
Cash Receipts Source Documents	5
Claim Files When Settled	10

<u>Type of Record</u>	<u>Years Recommended</u>
Construction Disbursements File	Permanent
Construction Projects Ledger	Permanent
Deposit Books and Slips	5
Employee Travel Expense Reports	5
Fixed Assets Ledger	Permanent
General Journal	Permanent
General Ledger	Permanent
General Source Documents	5
Journal Voucher File	5
Service Accounts Receivable Ledger	Permanent
Service Receipts File	5
Tax Accounts Receivable Ledger	Permanent
Tax Receipts File	5
Tax Assessor/Collector Reports	5
ADVERTISING	
Contracts With Engravers, Lithographers and Printers	5
Inquiries Record	1
Mailing Lists	Current
ENGINEERING	
Research Data and Feasibility Studies	20
Specifications, Installation Instructions, etc. (Pertaining to permanent structures)	Permanent
Engineering Reports (includes related correspondence)	Permanent
GENERAL RECORDS	
Annexation Files	Permanent
Authorizations for Expenditures	5

<u>Type of Record</u>	<u>Years Recommended</u>
Bonds, Surety	5
Correspondence	5
Charters	Permanent
Contracts and Agreements and Utility Commitments	20
Deeds and Easements and Consents To Encroachment	Permanent
Directors' Files	Permanent
1. Bonds, Oaths of Office, and Resignation Letters	
2. District Registration Forms	
District Status Reports	3
Election Files (Directors, Bond, Maintenance Tax, etc.)	Permanent
Fidelity Bonds of Employees	Permanent
Franchises	Permanent
Government Contracts and Subcontracts	5
Information Form File	Permanent
Insurance File	5
Leases	5
Minutes of Board of Directors' Meetings and Resolutions	Permanent
Notice of Meetings File (contains Certificates of Posting for courthouse and district)	Permanent
Official Minutes Files	Permanent
Operator's Reports	Permanent
Orders and Resolutions Files (except Rate Orders)	Permanent
Rate Order File includes Rules and Regulations and related affidavits of publication	Permanent
Voting Rights Act File	Permanent

<u>Type of Record</u>	<u>Years Recommended</u>
Waste Discharge Permits	Permanent
Water Well Permits	Permanent
INVENTORY AND COST RECORDS (other than property)	
Cost Production and Job Summary Records	5
Cost Reports and Statements	5
Cost Sheets	5
Labor Distribution Records	5
Price Records	5
Quotations	5
Specifications	5
LEGAL	
Case Files, Affidavits, Testimony, Depositions, Briefs	20
Legal Correspondence File	20
General Agreements	20
Patents, Patent Assessments, Patent Applications, Dockets	20
PAYROLL AND RELATED RECORDS	
Assignments, Attachments and Garnishments after settlement or termination	5
Employees' Deduction Authorizations--includes Rate Changes, Discharges, "Add to Payroll" Notices	5
Individual Employee Earnings Record	5
Labor Distribution Cost Records	5
Payroll Registers (gross and net)	5
Payments and Reports to Government - includes Federal, State and Municipal authorities covering payments and reports relating to Income Tax Withholdings, Contributions to FICA, Workmen's Compensation, reports on employees' earnings, etc.	5

<u>Type of Record</u>	<u>Years Recommended</u>
Retirement and Pension Plan Records (including deduction authorizations)	Permanent
Time Cards - time sheets	5
PERSONNEL	
Accident Reports	5
Applications for Employment (whether hired or not)	5
Disability and Sick benefits Records	5
Employee Contracts	5
Group Insurance Records	5
Individual Employee Personnel File	5
Invention Assignment Forms	Permanent
Old Age Benefit Reports	5
PURCHASING	
Acknowledgment of Orders	5
Contracts with Vendors	5
Correspondence with Vendors, etc.	5
Price List Files	5
Purchase Cost Records	5
Purchase Orders - filled and unfilled	5
Purchase and Priority Requisitions	5
Quotations (those acted upon)	5
Source of Supply and Catalogue Files	5
TRAFFIC, SHIPPING AND RECEIVING	
Bills of Lading	2
Claims	5

<u>Type of Record</u>	<u>Years Recommended</u>
Delivery Reports	3
Receipts for Registered Mail and Express Packages	1
Receiving Reports	3

APPENDIX K

Sample Request For Audit Proposal

XYZ UTILITY DISTRICT Any City, Texas

Date

CPA & Company
Certified Public Accountants
Any City, Texas

Gentleman:

The Board of Directors of XYZ Utility District invites your firm to submit a proposal to serve as auditor of the District. In accordance with the Professional Service Procurement Act (Article 664-4, Texas Revised Civil Statutes) we will be selecting an auditor on the basis of demonstrated competence and qualifications in water district auditing, at reasonable and fair fees.

We are prohibited from requesting, and you are prohibited from submitting, a competitive bid for this engagement. However, we do request that you include in your proposal a fee estimate in accordance with the most current Rules of Professional Conduct as promulgated by the Texas State Board of Public Accountancy, as follows:

1. A statement to the effect that the amount quoted is an estimate and that the auditor will not be bound to provide the services for the estimated amount.
2. The estimated number of people by classification to be involved in performing the work, and the range of education and experience in each classification.
3. The estimated time to be required for the engagement by personnel classification.
4. An estimated time schedule for the performance of the work.
5. The estimated audit fee based on the above work.

The fiscal year-end of XYZ Utility District is (month-end date) of each year. You may contact (name and phone number) to obtain information about the current status of the District.

(The Board should insert a closing statement giving instructions for number of copies of the proposals needed, deadline dates, Board meeting date, etc.)

Very truly yours,

XYZ Utility District
_____, President

APPENDIX L

Reports and Records

- I. **Tax Assessor/Collector's Report** - The purpose of the tax assessor/collector's report is to furnish the bookkeeper of a water district with the information required to properly book the district's tax assessments and collections. The information contained in the report should reflect all of the transactions through the last day of the district's accounting period. The report should contain:
 - A. Cash Receipts and Disbursements - All cash transactions should be reported and should be reconciled with beginning and ending cash balances.
 - B. Taxes Receivable - This section shows delinquent taxes receivable at the beginning of the tax year, plus the current year tax roll, plus or minus any adjustments to taxes during the fiscal year, less all collections during the fiscal year. Taxes receivable should be reported by years, and all changes should be shown. Collections should agree with all collections included in the cash receipts and disbursements section of the report.
 - C. Taxpayer Overpayments - The balance due to taxpayers at the beginning of the period should agree with the audit report. The balance due taxpayers should reconcile with the difference between overpayments collected and overpayments refunded. Collection and refund of overpayments should agree with the amounts included in the cash receipts and disbursements section of the report.
 - D. Tax Adjustments - All tax adjustments made after approval of the tax roll by the board of equalization should be reported for the current tax year and all prior years. It is recommended that these adjustments be approved by the board of directors. It is necessary to include the adjustments page only when changes are made.
 - E. Bank Reconciliation - The balance per the bank statement should be reconciled to the cash balance per the tax assessor-collector's report each month.
 - F. Accounts Payable - A list of all accounts payable for goods or services received during the year for which payment has not been made as of the end of the fiscal year should be furnished to the bookkeeper. This would include unbilled charges such as tax assessor fees, legal fees, etc.
- II. **Tax Assessor Collector - Minimum Record Requirements**
 - A. Board Folder
 - 1. Reports to the Board - All reports to the board during the fiscal year
 - 2. Tax Assessor's Contract
 - 3. Appraisal District's Approval of Original Roll
 - 4. Penalty and Interest Rates
 - 5. Tax Assessor's Bond

B. Tax Roll and Receipts

1. Original Roll - The original roll for each year the district has levied taxes
2. Delinquent Roll - A roll showing all outstanding taxes by years as of the fiscal year end date
3. Tax Receipts - Paid receipts grouped by date of deposit
4. Deposit Slips - Copy of deposit slip attached to applicable group of receipts

C. Bank Statement Folder

1. Bank Statements - Bank statements for all accounts maintained during the year
2. Bank Reconciliation - Monthly reconciliations for each bank account

D. Tax Assessor/Collector's Report - Revenues and expenses coded using numerical chart of accounts

III. **Operator/Billing Agent's Report** - The purpose of the operating report is to furnish the bookkeeper of a water district with the information required to properly record the district's water and sewer revenue transactions. The information enclosed is the minimum requirement; additional information may be requested. The accompanying list is not designed for an operator that pays operating expenses and maintains a general ledger for the district.

This information is to be used as a guide only and should be modified as appropriate to accommodate the needs of the district and the procedures of the companies providing the information.

However, if applicable information is deleted, the bookkeeper will not be able to properly record the water and sewer billings of the district.

The responsibilities for water and sewer billings are divided into two separate functions, operating and billing. The work may be done by one company or by two companies. The explanations that follow are based on the assumption that two companies are involved and that the records are computerized.

Typically, it is the function of the operator to manage the overall physical operations of the district's water and sewer system, to install taps, read meters and maintain records of taps installed. The operator or billing agent may collect and deposit tap fees.

The billing agent sends monthly bills to the customers of the district based on information furnished by the operator, collects payments from customers, follows up collection of delinquent accounts, collects and refunds deposits, reports billing and statistical information to the board of directors and maintains all applicable accounting records. The billing agent may maintain an interim cash account or may deposit directly to an account maintained by the district's bookkeeper. The Operator's Report should contain:

A. Accounts Receivable Analysis - The information needed for the preparation of the accounts receivable analysis section comes directly from the recap of billings. Normally, the categories included in this report will be sufficient to report the revenue transactions of the district. However, the transactions of the district are not limited to those included in this report. Significant or unusual billing adjustments should be explained to the board of directors.

- B. Collection Analysis - The billing agent needs to report to the bookkeeper all deposits that have been made by the billing agent. All items that are not included in the billing run would be shown as a separate line item. To reconcile to the total amount deposited by the billing agent (for the calendar month which includes all deposits made during the month, whether or not they cleared the bank), the following items must be considered:

1. Add returned checks that have been redeposited and identified separately.
2. Accounts receivable collections that were received after the date of the billing run, but prior to the end of the month, need to be added.
3. Accounts receivable collections that were received after the date of the prior billing run, but prior to the end of the preceding month, need to be subtracted.

In subsequent months, the amount described in number 2 above would become the amount described in number 3.

- C. Tap and Customer Information - Taps installed and taps collected should be furnished through month end. Meters installed should include only those meters that were installed prior to the meter reading date. All double taps should be counted as two installations. At the end of the fiscal year, meters installed should be updated to the end of the applicable month. The difference between taps collected and installed and meters installed should agree with the applicable lists furnished to the bookkeeper by the operator. The number of customers billed for service should be reconciled with the number of meters installed to date on a monthly basis. The number of customers billed is customers billed for service counting an address only once (i.e., exclude double billings for transfers, etc.). Add customers for which a meter has been installed, but not billed during the month (i.e., vacant houses and meters installed during the month that were not billed for service until the following month, etc.).

- D. Customer Deposits - The customer deposit section is a recap of customer deposit transactions for the month. Because of the varying deposit policies of districts, the number of deposits on hand may not agree with the number of customers being billed.

The adjustments line on the report should include such items as billing corrections which directly reduce the receivables from customers. Preferably, whenever a deposit is to be offset against a final bill, a check should be issued to the customer for the excess of the deposit over the final bill and another check should be written to the district for the amount of the final bill and treated as a collection by the district. When the receivable is equal to or greater than the deposit, a check should be written only to the district.

- E. Bank Reconciliation and Proof of Cash - When the billing agent maintains an interim bank account, a bank reconciliation and proof of cash are necessary in order for the bookkeeper to properly record all transactions of the interim account.

The purpose of the proof of cash section is to reconcile the total deposits reflected on the bank statement to the collections report. It is also used to reconcile the disbursements per the bank statement of an interim account to the transfers to the operating account maintained by the bookkeeper. Without this information, the bookkeeper cannot properly record cash and revenues. Deposits in transit and outstanding checks should be taken from the current and prior month's reconciliation.

- F. Returned Checks - The billing agent should furnish a list to the bookkeeper of all returned checks on and at the end of the month. This list will enable the district's bookkeeper to properly reconcile the amount of returned checks booked in the general ledger.
- G. Allowance for Doubtful Accounts - At the end of the district's fiscal year, the billing agent should furnish a list to the bookkeeper of accounts for which collection is doubtful. This list will enable the bookkeeper to determine whether and for what amount an allowance should be established.

IV. **Operator** - Minimum Record Requirements

- A. Tap Log - The tap log should contain the following information:
 - 1. The date the cash was received for the tap.
 - 2. The name of the person or company ordering the tap.
 - 3. The service address and legal description of where the tap is to be installed.
 - 4. The date the tap was installed.
 - 5. The serial number of the meter installed on the tap.
 - 6. The account number for billing assigned to that service address.
 - 7. The date the cost of the tap installation was billed to the district.
 - 8. The receipt number and amount received for the tap installation.
 - 9. The date the sewer inspection was performed.
- B. Meter Books - The meter books should include all customers of the district, including standby customers by service address with the previous and current reading. After the operator has completed the meter readings, the books should be returned to the billing agent.
- C. Damage Claims
 - 1. Invoices and supporting documentation relative to damages to the district's system by contractors, etc.
 - 2. If the operator is designated by the board to collect billings, subledger records relative to billings and collections should be maintained.
- D. Other
 - 1. Map of the District - All lots marked with an account number in an order that will facilitate reading all meters.
 - 2. Tap Installation Work Order - Work order showing where a tap is to be installed, who ordered the tap, when the tap fee was received, receipt number and amount received.

E. Information to be Furnished to the Billing Agent

1. Tap and meter information as follows for the current month and to date:
 - a. Number of taps installed through month end.
 - b. Number of tap fees collected through month end.
 - c. Number of meters installed prior to meter reading date.
2. Meter books
3. Damage claim invoices and collection information, if these amounts are to be billed and collected by billing agent.

F. Information to be Furnished to Bookkeeper

1. At year end, list by address of taps installed, not collected (double taps).
2. At year end, list by address of taps collected, but not installed.
3. At year end, list by address of taps installed where no meter has been installed.
4. Damage claim invoices and collection information if these amounts are to be billed and collected by the bookkeeper.

V. **Billing Agent** - Minimum Record Requirements

A. Board Folder

1. Rate Orders - All rate orders that were in effect during the year should be included in the folder.
2. Report to the Board - All reports to the board of directors during the fiscal year should be included in their folder.

B. Meter Books

1. Regular Customers - All meter reading sheets for regular customers.
2. Standby Customers - All customers being billed standby charges listed by lot.

C. Billing Ledger or Workbook - Water and Sewer Billings - All records for water and sewer billings and collections, including:

	<u>Explanation</u>
1. Recap of Billings	Categorical breakdown of billings and collections for the month, including the beginning and ending receivable and an aged analysis of the ending receivable.
2. Listing of Accounts Receivable	All receivables by customer account numbers, including service address, name, billing address and total.
3. Adjustment Information	Recap of all adjustments to the accounts receivable, including an explanation for each adjustment.
4. Meter Reading Information	List of unusually high or low usage readings, reverse readings and other adjustments in meter readings which are used to determine the proper usage billing to customer. Any change made to the meter readings should be fully explained.
5. Security Deposits	List by customer of security deposits on hand, including total.
6. Statistical Information	Recap of number of customers within the district, both billed and nonbilled, and the number of gallons billed. Reconciliation of customers billed to meters installed.

D. Bank Statement Folder - To be maintained when the billing agent maintains bank accounts:

1. Bank Statements - Bank statements for all accounts maintained during the fiscal year.
2. Bank Reconciliations - Monthly reconciliations for each bank account.

E. Billing Envelope

1. Deposit Slips - All deposit slips for each month should be included.
2. Stubs - All payment stubs for water and sewer billing which relate to the deposit slips should be included. A tape of the stubs should be attached to each group to reconcile to the deposit slips.

F. Damage Claims

1. Invoices and supporting documentation.
2. When damage claims are not included in billings described above and the billing agent is responsible for maintaining the information:

- a. Subledger records relative to billings and collections.
- b. Billing and collection totals should be furnished to the bookkeeper monthly.

G. Information to be Furnished to Bookkeeper

1. Monthly operating report, together with applicable attachments;

-or-

2. Annual financial statements for the general fund if applicable revenues and expenditures are recorded and reported by the billing agent.
3. Damage claim information if excluded from reports listed above.

H. Standby Charges - The following records (described in detail above), if not included in normal billing cycle:

1. Recap of Billings
2. Listing of Accounts Receivable
3. Adjustment Information

APPENDIX M

Special Journals Reconciled Monthly Bank Statements

Usually the bookkeeper is responsible for preparing the monthly bank account reconciliation for each of the water district's bank accounts. The reconciled statement should then be reviewed by a second person to verify the accuracy of the reconciliation. The following sequence of steps takes place in preparing the monthly bank account reconciliations for a manual system.

PERFORMED BY: Designated Bookkeeper

1. Obtain a bank account reconciliation form, or use the form supplied by the bank usually found on the back of the statement. **An example of a bank reconciliation form can be found at the end of this section of the appendix.**
2. Enter the bank name and the title of the bank account being reconciled in the space labeled "Bank Name/ Bank Account Title".
3. Enter the Fund name and the title of the cash account being reconciled in the space labeled "Fund Name/ Cash Account Title".
4. Enter the bank statement date in the space labeled "Date"
5. Enter the ending bank account balance, per the bank statement, on the line labeled "BALANCE PER BANK" in the right-hand column.
6. For each deposit not received by the bank but recorded on the books, enter the deposit slip number and the date of the deposit on the lines labeled "Deposit No./Date". Enter the amounts of these deposits on the corresponding lines in the left-hand column. These are the outstanding deposits, or deposits in transit.
7. Enter any other reconciling items that have been recorded on the books but not by the bank that would increase the bank balance on the line labeled "Other". Enter a description of the reconciling item on the "Other" line and enter the amount in the left-hand column.
8. Compute the sum of the items in the left-hand columns and enter the result on the "Total Additions" line in the right-hand column.
9. Add the amount labeled "Total Additions" to the amount labeled "BALANCE PER BANK" and enter the sum in the right-hand column on the next line in the space beside the dollar sign (\$).
10. Enter the check number of all checks written that are not included in the bank statement on the lines labeled "No.", and enter the corresponding amounts in the left-hand column. These are the outstanding checks. Checks outstanding from the prior month that are not included on the current bank statement should also be included here.
11. Enter any other reconciling items that have been recorded on the books but not by the bank that would decrease the bank account balance on the line labeled "Other". Enter a description of the reconciling item on the "Other" line and enter the amount in the left-hand column.

12. Compute the sum of the items in the left-hand column under the "Deductions" heading and enter the result on the "Total Deductions" line in the right-hand column.
13. Subtract the amount labeled "Total Deductions" from the sum of the amounts labeled "Total Additions" and "BALANCE PER BANK" and enter the result on the line labeled "Adjusted Bank Balance".
14. Enter the previous month's reconciled balance on the line labeled "BALANCE PER BOOKS LAST MONTH".
15. Enter the amount of any interest earned on certificates of deposit that is automatically credited to the checking account by the bank (if any) on the line labeled "Interest on C.D. Credited by Bank" in the left-hand column.
16. Enter a description of any errors made on the books that, when corrected, would increase the book cash balance on the line labeled "Error in Books". Enter the corresponding correcting amount in the left-hand column.
17. Enter any other reconciling items that have been recorded by the bank but not on the books that would increase the book cash balance on the line labeled "Other". Enter a description of the reconciling item on the "Other" line and enter the amount in the left-hand column.
18. Enter the total amount of cash receipts (deposits) recorded on the books for the month.
19. Compute the sum of the items in the left-hand column and enter the result on the "Total Additions" line in the right-hand column.
20. Add the amount labeled "Total Additions" to the amount labeled "BALANCE PER BOOK LAST MONTH" and enter the sum in the right-hand column on the next line in the space beside the dollar sign (\$).
21. Enter the amount of the bank service charge deducted from the checking account on the line labeled "Bank Service Charges". Enter the amount in the left-hand column beside the dollar sign (\$).
22. Enter the amount of any other charges made to the checking account by the bank on the line labeled "Other Bank Charges". Enter the amount in the left-hand column.
23. Enter the total of returned checks which have not been recorded on the books of the District on the line labeled "Unrecorded Returned Checks" in the left-hand column.
24. Enter a description of any errors made on the books that, when corrected, would decrease the book cash balance on the line labeled "Error in Books". Enter the corresponding correcting amount in the left-hand column.
25. Enter the total amount of all cash disbursements recorded on the books for the month.
26. Enter any other reconciling items that have been recorded by the bank but not on the books that would decrease the book balance on the line labeled "Other". Enter a description of the reconciling item on the "Other" line and enter the amount in the left-hand column.

27. Compute the sum of the items in the left-hand column under the “Deductions” heading and enter the result on the “Total Deductions” line in the right-hand column.
28. Subtract the amount labeled “Total Deductions” from the sum of the amounts labeled “Total Additions” and “BALANCE PER BOOKS LAST MONTH” and enter the result in the line labeled “Adjusted Book Balance”.
29. Verify that the amounts labeled “Adjusted Bank Balance” and “Adjusted Book Balance” are equal. Resolve all discrepancies before continuing.
30. File the completed bank account reconciliation.

COMPUTERIZED SYSTEM

The steps mentioned above are not necessary for a computerized reconciliation. However, a computerized reconciliation must detail all outstanding cash receipts, outstanding cash disbursements, and any bank account adjustments. The reconciled bank statement must agree to the checkbook.

EXAMPLE

Bank Account Reconciliation
(Bank Name/Bank Account Title)
(Fund Name/Cash Account Title)
(Date)

BALANCE PER BANK:		\$
Additions:		
Deposits in Transit		
Deposit No./Date	\$	
Deposit No./Date		
Deposit No./Date		
Deposit No./Date		
Other (Specify)	_____	
Total Additions		_____
		\$
Deductions:		
Outstanding Checks		
No.	\$	
No.		
No.		
No.		
Other (Specify)	_____	
Total Deductions		_____
ADJUSTED BANK BALANCE		<u>\$</u>
		<u> </u>
BALANCE PER BOOKS LAST MONTH:		\$
Additions:		
Interest on C.D. Credited by Bank	\$	
Error in Books (Specify)		
Other (Specify)		
Cash Receipts	_____	
Total Additions		_____
		\$
Deductions:		
Bank Service Charges	\$	
Other Bank Charges		
Unrecorded Returned Checks		
Error in Books (Specify)		
Cash Disbursements		
Other (Specify)	_____	
Total Deductions		_____
ADJUSTED BOOK BALANCE		<u>\$</u>
		<u> </u>

Special Journal

Current Investment Journal

Once a district begins receiving money, the district has an obligation to spend or invest that money wisely. There are various sources for a district's money supply. Some of the major sources include water and wastewater revenues, developer advances, proceeds from the sale of bonds or BANS, and tax revenues.

An undeveloped district may sell bonds to finance the construction of water, wastewater and drainage facilities. Any money remaining after TNRCC approved expenses from the bond sale must be invested. However, money invested cannot earn interest at an interest rate that exceeds the net effective interest rate on the bonds.

Principal and interest on the bonds is usually payable from the proceeds of an annual ad valorem tax levied against taxable property in the district. Sometimes, net revenues from the operation of a district's water and wastewater system may be used. Funds for payment of bonds can also be derived from surcharges. District revenues should be invested to earn the district as much money as possible subject to the net effective interest rate on the bonds.

Statutes authorize the district to invest and reinvest in direct or indirect obligations of the United States, the State of Texas, or any county, city, school district, or other political subdivision of the state. Funds of the district may be placed in certificates of deposit of state or national banks or savings and loan associations within the state provided that they are secured in the manner required for the security of the funds of counties in the State of Texas. Additional authorized investments are detailed in **Appendix C**.

In accordance with state statutes, the district should require that security be provided by depositories for all funds held by them. The depository should provide security for any amount in excess of the insured amount (**Appendix E**). However, the designated investment officer must request the pledging of these securities. For additional information, see **Appendix D**.

Investments are usually in the form of money markets, certificates of deposit, treasury bills or pooled investments. Money market accounts will usually generate a monthly statement that can be reconciled. No monthly statement is kept for each certificate of deposit or treasury bill (T-Bill). Information needed for a current investment journal includes the following:

1. Certificate of deposit or T-Bill number.
2. Name of depository.
3. Dates of purchase and maturity.
4. Amount invested.
5. Interest rate.
6. Origin of funds.
7. Interest earned at maturity.
8. Amounts renewed or transferred to other accounts.

APPENDIX N

FILING INSTRUCTIONS for TEXAS WATER DISTRICTS

These instructions are summaries. For further details, refer to the Texas Water Code, Section 49.191-.198 and the Annual Audit Report Requirements (AARR). **File the document below:**

DOCUMENT:	<u>Financial Dormancy Affidavit</u> *	<u>Annual Financial Report</u> *	<u>Audit Report</u>
<u>IF</u>	<ul style="list-style-type: none">- Your district had \$500 or less of receipts from operations, tax assessments, contributions, loans or any other sources during the calendar year.- <u>and</u> the district had \$500 or less of disbursements of funds during the calendar year;- <u>and</u> the district had no bonds or other long-term (more than one year) liabilities outstanding during the calendar year;- <u>and</u> no cash or investments that exceeded \$5,000 at any time during the calendar year.	<ul style="list-style-type: none">- Your district does not collect taxes;- <u>and</u> your district had no bonds or other long-term (more than one year) liabilities outstanding during the fiscal period;- <u>and</u> gross receipts from loans, operations or contributions did not exceed \$100,000 during the fiscal period;- <u>and</u> the district's cash and temporary investments were not in excess of \$100,000 at any time during the fiscal period.	<ul style="list-style-type: none">- Your district does not qualify to file a Financial Dormancy Affidavit or an Annual Financial Report, then the district must engage a Texas CPA or PA (with a current license) to perform an audit.
<u>DUE WHEN</u>	<u>Annually</u> , on or before Jan. 31. The Financial Dormancy Affidavit form refers to the calendar year (January 1 through December 31).	<u>Annually</u> , within 45 days after the close of the district's fiscal year.	<u>Annually</u> , within 135 days after the close of the district's fiscal year.
<u>FILE</u>	<ul style="list-style-type: none">- File one copy in the district's office.- File one copy with the Reports and Supervision Team, Water Utilities Division, Texas Natural Resource Conservation Commission.		
<u>ALSO</u>	<ul style="list-style-type: none">- File one copy of the Annual Filing Affidavit* with the Reports and Supervision Team, Water Utilities Division, TNRCC, at the same time the Audit Report is filed. That affidavit certifies that all required documents have been filed with the district. While the Annual Filing Affidavit is a separate form that must be submitted with an Audit Report, it has been incorporated within the Financial Dormancy Affidavit and the Annual Financial Report forms for user convenience.		

OUR MAILING ADDRESS IS:

**Reports and Supervision Team, MC-152
Water Utilities Division
Texas Natural Resource Conservation Commission
PO Box 13087
Austin TX 78711-3087

Phone (512) 239-6170**

* Copies of these forms can be obtained by contacting the Reports and Supervision Team at 512/239-6170.

APPENDIX O

SAMPLE CODE OF ETHICS

AND POLICIES RELATING TO TRAVEL EXPENDITURES, DISTRICT
INVESTMENTS, PROFESSIONAL SERVICES, AND FISCAL MANAGEMENT
FROM THE OFFICE OF THE STATE AUDITOR-SAO REPORT NUMBER 9-064
(AS AMENDED FOR LEGISLATIVE CHANGES)

DEFINITIONS

As used in these guidelines:

District

The term “district” shall mean and refer to any district or authority created by authority of either Article III, Section 52, Subsection (b), Subdivisions (1) and (2), or Article XVI, Section 59, of the Texas Constitution.

Board

The term “board” shall mean and refer to the governing body of the district (board of directors).

Director

The term “director” shall mean a person elected or appointed to serve on the board of directors of the district.

District Officials

The term “district officials” shall mean district directors, officers, employees, and persons and business entities engaged in handling investments for the district as representatives of the district.

Employee

The term “employee” shall mean any person employed by the district, but does not include independent contractors or professionals hired by the district as outside consultants.

Substantial Interest

The term “substantial interest” shall mean that as defined by current State law as of the date of adoption of this code of ethics, Chapter 171 of the Local Government Code regulating conflicts of interest of district officials.

ARTICLE I

Code of Ethics

1.01. Purpose

This code of ethics has been adopted by the district for the following purposes: (a) to comply with section 49.199 of the Texas Water Code, as amended; (b) to encourage high ethical standards in official conduct by district officials; and (c) to establish guidelines for such ethical standards of conduct.

1.02. Policy

It is the policy of the district that district officials shall conduct themselves in a manner consistent with sound business and ethical practices; that the public interest shall always be considered in conducting district business; that the appearance of impropriety shall be avoided to ensure and maintain public confidence in the district; and that the board shall control and manage the affairs of the district fairly, impartially, and without discrimination, and in accordance with the stated purpose of the district.

1.03. Qualification of Directors

- A. A person shall not serve as a director if he or she is not qualified to do so under the provisions of the district's enabling legislation.
- B. Within 60 days after the board determines that any director is not qualified to serve on the board, it shall replace such director with a person who is qualified.
- C. Any director not qualified to serve on the board, who willfully occupies an office and exercises the duties and powers of that office, may be subject to penalties under the Texas Water code, including possible conviction of a misdemeanor and imposition of a fine.

1.04. Conflicts of Interest

- A. A district official is prohibited by Chapter 171 of the Local Government Code from participating, directly or indirectly, in a vote or decision or from acting as a surety on any matter involving a business entity in which the official has substantial interest, if it is reasonably foreseeable that an action on the matter would confer an economic or any other benefit on the business entity.
- B. In cases of conflicts of interest, district officials shall disclose such conflicts and shall file with the board secretary an affidavit stating the nature and extent of the conflict of interest. Thereafter, that district official shall abstain from participation in the matter as provided by law.
- C. District officials shall not disclose, without written legal authorization, confidential information to advance the financial or other private interests of himself or others regarding any contract or transaction which is or may be the subject of an official action of the district.
- D. The district may not contract for the purchase of services or personal property directly with a district official or with a business entity in which a district official has a substantial interest except as permitted by law.

- E. The board shall take a separate vote on any budget item specifically dedicated to a contract with a business entity in which a director has a substantial interest. The director having the substantial interest may not participate in that separate vote, but may vote on a final budget if the separate budget item voted on does not exceed 10% of the total budget.

1.05. Nepotism

The board shall not confirm the appointment to any position, nor award a contract, to a person related to a member of the board within the second degree by affinity (marriage) or within the third degree by consanguinity (ancestry) when the salary or other compensation of such appointee is paid, directly or indirectly, from district funds, except as provided by Tex. Rev. Civ. Stat. Ann. art. 5996(a) (Vernon Supp. 1988).

1.06. Acceptance of Gifts

- A. A district official shall not solicit, accept, or agree to accept any benefit of value from a person or business entity the district official knows is interested in or likely to become interested in any contract, purchase, payment, claim, or other transaction involving the exercise of their discretion as a public servant, or any matter before the board, or likely to come before the board for any decision, opinion, recommendation, or vote.
- B. The prohibition against gifts or favors in section 1.06(a) shall not apply to:
 - (1) an occasional non-pecuniary gift, valued at less than \$25.00; or
 - (2) an award publicly presented in recognition of public service.

1.07. Use of District Property

No board member, officer, or employee shall permit any personal or unauthorized use of district-owned or district-controlled, equipment materials, supplies, or property.

ARTICLE II

Travel Expenditures Policy

2.01. Purpose

The board hereby establishes policies for reimbursing district directors, officers, and employees for necessary and reasonable travel expenses incurred while conducting business or performing official duties or assignments.

- A. Authorized expenses include cost of meals, lodging, commercial travel, in some cases personal automobile mileage, and other necessary and reasonable costs incurred while on official business away from designated headquarters.
- B. Reimbursement for travel expenses shall be subject to approval by the board. The reimbursement request shall include a statement of the business purpose of the travel, date, time, and place, and shall be accompanied by supporting receipts and invoices as required by the board.

2.02. Per Diem

District directors shall be entitled to compensatory per diem for days spent on official business in the amount prescribed by law, not to exceed the number of days prescribed in the district's enabling legislation, in addition to reimbursement of actual expenses for meals, lodging, and transportation as discussed in sections 2.03 and 2.04 below.

2.03. Meals and Lodging

Unless further restricted by legislation, reimbursement to directors for actual expenses for meals and lodging shall not exceed the maximum amount allowed for state legislators.

2.04. Transportation

Directors or employees who use personal vehicles while on district business travel may be reimbursed for actual miles driven at the current rate allowed by the Internal Revenue Service. Mileage will be computed by the most direct route, and the use of personal vehicles for district travel must be approved by the board in advance. Directors or employees traveling by commercial transportation are entitled to reimbursement of the actual cost of necessary transportation for performing official business, except the reimbursement for air transportation shall not exceed the next lowest available airline fare below first class unless such is not available.

ARTICLE III

Investments

3.01. Purpose

This policy with respect to district investments has been adopted to establish the principles and criteria by which the funds of the district should be invested and secured (a) to preserve the principal, (b) to earn interest, and (c) to comply with various provisions of Texas law relating to the investment and security of funds of districts ("Investment Laws"). As of the date of the adoption of these policies, sections 49.156 and 49.157 of the Texas Water Code, articles 2529b-1 and 4413(34c) of the Texas Revised Civil Statutes, Chapter 116 of the Local Government Code, and any other appropriate statutes are applicable to the investment of the district's funds.

3.02. Policy of Investment

- A. The preservation of the district's principal shall be the primary concern of the district officials who are responsible for the investment of district funds. To the extent that the principal is protected, district funds shall be invested to yield the highest possible rate of return, taking into consideration the strength of the financial institution, and complying with any Internal Revenue Code laws or regulations and procedures set forth in any bond resolutions or orders, adopted from time to time by the Board, requiring yield restrictions. Funds of the district shall be invested by the district's officials in accordance with this policy. Any resolution or order adopted by the board relating to investment policies or procedures shall be in writing and shall be made available to requesting members of the public.

- B. District funds shall be invested and reinvested by the district's investment officer only in national or state banking associations or savings and loan associations located within the State of Texas ("Texas financial institutions"), or, in federal treasury bills. The principal, plus accrued interest, invested in financial institutions in accordance with this policy shall not exceed the FDIC or FSLIC insurance limits or exceed the collateral (as such term is hereinafter defined) pledged as security for the district's investments.
- C. It shall be the responsibility of the district's investment officer to invest and reinvest the district funds in accordance with this policy to meet the needs and requirements of the district. It shall be the policy of the district that funds shall not remain in any given investment for longer than two years. The board, by separate resolution, may provide that the investment officer may withdraw or transfer funds from and to accounts of the district on such terms as the board considers advisable. Providing however, that nothing hereinabove provided shall authorize any transfer, expenditure, or appropriation of district funds, other than for the district's own account, unless by check or draft signed by three (3) members of the board of directors or as authorized by separate order or resolution of the board.
- D. Funds in the district accounts shall be invested by the district's investment officer as follows:
 - 1. Construction or Capital Projects Account: Funds in this account shall be invested in accordance with any applicable orders of the Texas Natural Resource Conservation Commission to meet the construction needs of the district as determined by the district's engineer. The engineer shall submit to the board semi-annual written reports stating the anticipated construction needs of the district for the succeeding 12 months.
 - 2. Debt Service Account: Funds in this account shall be invested to meet the debt service requirements of the district and to comply with the district's bond resolutions or orders.
 - 3. Operating or General Account: Funds in this account shall be invested to meet the operating requirements of the district as determined by the annual operating budget of the district, or by resolution of the board.
- E. Should total district funds exceed \$ XX,XXX, there is hereby established an investment committee, composed of the district's investment officer, the district's financial advisor, and at least one director. The investment committee shall meet quarterly to monitor and review the investments and collateral of the district. The investment officer shall be the chairman of the committee. The committee shall report concerning the district's investments transaction for the preceding year describing the investment position of the district at the end of each fiscal year. The report shall be signed by the members of the committee. The committee also shall report to the board on its review the month following each quarterly meeting.

3.03. Security of District Funds

- A. It shall be the policy of the district that all funds shall be insured by the FDIC, FSLIC, or by collateral pledged to the extent of the fair market value of the amount not insured. The district officials recognize that FDIC and FSLIC insurance is only available up to a maximum of \$ 100,000 (including accrued interest) and that the amount of funds at any one Texas financial institution (including branch banks located within the same county) will be cumulated to determine the maximum amount of insurance coverage.

- B. To the extent district funds are not insured by the FDIC or FSLIC, there shall be pledged as collateral, to the extent of the market value thereof, any of the following securities: (1) government securities or obligations issued by the State of Texas, its agencies or political subdivisions, and approved by the Attorney General of Texas payable from taxes or revenues, approved by the investment committee; or, (2) direct obligations of the United States of America backed by the full faith and credit of the government; or, (3) any other obligations or securities authorized to be collateral securing funds of districts under the laws of the State of Texas, approved by the investment committee (collectively, the “collateral”).
- C. The investment committee shall review the fair market value of the collateral pledged to secure the district’s funds on a quarterly basis to ensure that the district’s funds are fully secured. The investment committee shall report to the board on its review the month following each quarterly meeting.
- D. There shall be no sharing, splitting or cotenancy of collateral with other parties or entities. The investment officer shall ensure that the custodian of the collateral shall be an independent third party Texas financial institution and that the collateral shall be pledged only to the district; the investment officer shall obtain safe-keeping receipts from the Texas financial institution regarding same.

ARTICLE IV

Professional Services Policy

4.01. Purpose

This professional services policy has been adopted to provide for the selection, monitoring, review, and evaluation of the district’s professional services contracts. Consultants retained by the district to provide professional services include, but are not limited to, legal, engineering, financial advisor, management, bookkeeping, auditing, and tax collecting. Selection of such consultants shall be based upon their qualifications and experience.

4.02. Periodic Review

The performance of the consultants providing professional services to the district shall be regularly monitored and reviewed by the board, and the board may appoint a professional services committee to provide such monitoring and review to the board.

ARTICLE V

Management Policy

5.01. Purpose

The board desires to adopt a policy to ensure better use of management information, including the use of budgets in planning and controlling costs, the establishment of a functioning audit committee, and the use of uniform reporting requirements.

5.02. Accounting Records

District accounting records shall be prepared on a timely basis and maintained in an orderly manner, in conformity with generally accepted accounting principles and the requirements of the Texas Natural Resource Conservation Commission. Such records shall be available for public inspection during regular business hours at the district's office.

5.03. Audit Requirements

- A. Unless otherwise exempted by the rules of the Texas Natural Resource Conservation Commission as described in 5.03(C), the district's fiscal accounts and records shall be audited annually in accordance with State law governing the audits of water districts, at the expense of the district, by a certified public accountant familiar with the Texas Natural Resource Conservation Commission's rules, regulations, standards, and guidelines applicable to water district audits. As of the date of adoption of these policies, sections 49.191-49.200 of the Texas Water Code and 30 Texas Admin. Code section 293 (Rules of the Texas Natural Resource Conservation Commission) govern the audits of water districts (the "Audit Laws").
- B. The audit shall be completed and filed within the time limits established by the Audit Laws. Copies shall be filed with the Texas Natural Resource Conservation Commission together with an annual filing affidavit in the form prescribed by the Audit Laws. In the event the board refuses to approve the annual audited report, the district shall file a statement with the audit which explains the reasons for disapproval of the audit.
- C. If the district does not have sufficient revenues or activity so that it meets the requirements of the Audit Laws for financially dormant or inactive districts, it may prepare and submit an annual financial dormancy affidavit or an annual financial report described in the Audit Laws.
- D. If the district violates the Audit Laws, it may be subject to a civil penalty.

5.04. Audit Committee

The board shall establish an audit committee comprised of a least two directors and such persons as the board may deem appropriate. The persons selected should not be directly responsible for work subject to the audit. The audit committee shall conduct, at a minimum, an annual review of the district's financial status. The committee shall monitor variances from the district's budget, and shall make recommendations thereon to the board. The committee shall also review the annual district audit, and shall make recommendations thereon to the board.

5.05. Budget

The district shall annually adopt a budget in accordance with Rule 30 of the Texas Administrative Code, Section 293.97 (b), for use in planning and controlling district costs. Such budget shall take into consideration all district revenues, including, but not limited to, utility fees, taxes and surcharges, if any, and all projected district obligations and expenditures. The budget may be amended at any time but such amendment shall be approved in advance by the board. The manager of the district may have the authority to reallocate up to 10% of any line item between budget lines, as approved by the board.

ARTICLE VI

Miscellaneous

6.01. Gender

Any references herein to the masculine gender shall also refer to the feminine gender in all appropriate cases.

6.02. Open Meeting

The board officially finds, determines, and declares that these code of ethics and policies were reviewed, carefully considered, and adopted at a regular meeting of the board on ___, 19__, and that a sufficient written notice of the date, hour, place, and subject of this meeting was posted at a place readily accessible and convenient to the public within the district and on a bulletin board located at a place convenient to the public in the ___ County courthouse for the time required by law preceding this meeting, as required by the Open Meetings Law, Article 6252-17, Vernon's Texas Civil Statutes, as amended, and that this meeting had been open to the public as required by law at all times during which these code of ethics and policies were discussed, considered, and acted upon. The board further ratifies, approves and confirms such written notice and the contents and posting thereof.

Adopted the _____ day of _____, 19_____.

Signed the _____ day of _____, 19_____.

President
Board of Directors

Vice President
Board of Directors

Secretary/Treasurer
Board of Directors

Notary Public's Signature

(SEAL)